86-583

Supreme Court, U.S.
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NO. _____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

JIM AUSTIN AND AULEMIC, INC.,
Petitioners,

v.

LEXINGTON INSURANCE COMPANY,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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QUESTIONS PRESENTED FOR REVIEW

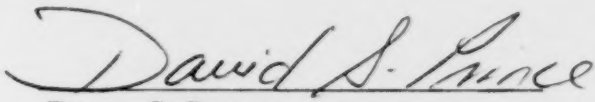
1. Did the court of appeals err in refusing to apply a controlling Texas statute to a marine insurance policy as mandated by Congress in the McCarran Act and by this Honorable Court in *Wilburn Boat Company v. Fireman's Fund Insurance Company*, 348 U.S. 310 (1955) and *Hooper v. California*, 155 U.S. 648 (1894).

2. By reaching out to decide a question of Texas state law currently pending before that state's highest court, did the court of appeals violate fundamental principles of federalism dictated by the United States Constitution, the McCarran Act, and the decisions of this Honorable Court.

CERTIFICATE OF INTERESTED PERSONS

The undersigned, counsel of record, certifies that the following list of parties have an interest in the outcome of this case.

1. Respondent, Lexington Insurance Company
2. Vinson & Elkins
3. Petitioners, Jim Austin and Aulemic, Inc.
4. Lorance & Thompson



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OPINIONS BELOW

The opinion of the court of appeals (App. A) is reported at 794 F.2d 941. The opinion of the district court (App. B) is reported at 610 F. Supp. 229.

JURISDICTION

The judgment of the court of appeals was entered on July 2, 1986. A timely suggestion of rehearing en banc was denied on August 4, 1986 (App. C). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1) (1982).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Amendment IX of the Constitution of the United States provides in pertinent part:

> The enumeration in the Constitution of certain rights shall not be construed to deny or disparage others retained by the people.

Amendment X of the Constitution of the United States provides in pertinent part:

> The powers not delegated to the United States by the Constitution nor prohibited by it to the states, are reserved to the states respectively or to the people.

The McCarran Act, 15 U.S.C. § 1011 (1945) provides in pertinent part:

> Congress declares that the continued regulation and taxation by the several States of the business of insurance is in the public interest, and that silence on the part of Congress shall not be construed to impose any barrier to the regulation or taxation of such business by the several States.

The McCarran Act, 15 U.S.C. § 1012 (1945) provides in pertinent part:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

STATEMENT OF THE CASE

This is a shipowner's action against a marine hull insurer which unlawfully denied the vessel owner's claim for damages under a hull insurance policy issued by the insurer. The vessel was owned and operated at the time of the loss by Jim Austin and his wholly-owned corpora-

tion, Aulemic, Inc., and was insured with Lexington Insurance Company. While under a long-term charter to Servac Shipping Line, Ltd., the ship suffered a casualty and Austin, the shipowner, requested his hull insurer, Lexington Insurance Company, provide coverage for the necessary repairs. Lexington denied coverage the day after the loss was reported based on a misstatement of maritime law and summarily closed its claim file. As a result thereof, Servac refused to continue with the long-term charter and the shipowner was subsequently forced to sell his vessel unrepaired for salvage.

The action was brought in the United States District Court for the Eastern District of Texas. The district court, sitting in admiralty entered judgment in favor of Austin and Aulemic, Inc. against Lexington for the reasonable cost of repairs owed under the policy, plus treble damages under Article 21.21 § 16 of the Texas Insurance Code and stipulated attorney fees. The court of appeals affirmed the district court's award of damages against Lexington for the reasonable cost of repairs and for attorneys fees, but refused to apply the controlling Texas Statute and reversed the district court's award of treble damages based on that Statute.

ARGUMENT

REASONS FOR GRANTING THE WRIT

I.

The opinion of the court of appeals in this case refusing to apply the Texas Insurance Code to a marine insurance policy has cast aside more than a century of uniform precedents of this Court interpreting marine insurance policies and the express policy mandated by Congress in the McCarran Act. Even before this Court's

opinion in *Paul v. Virginia,* 75 U.S. 168 (8 Wall.) 168 (1869), the power to regulate the insurance business had been left to the States. As early as 1894, this Court applied this rule to marine insurance policies in *Hooper v. California,* 155 U.S. 648 (1894). This Court has succinctly summarized the origin of insurance law in this country:

> The whole judicial and legislative history of insurance regulation in the United States warns us against the judicial creation of admiralty rules to govern marine policy terms and warranties. The control of all types of insurance companies and contracts has been primarily a state function since the States came into being.[1]

Although Congress recognized that marine insurance companies were operating under state laws as early as 1920,[2] it was the passage of the McCarran Act[3] in 1945 which expressly set forth Congress' intent that "the business of insurance . . . shall be subject to the laws of the several states which relate to the regulation or taxation of such business." 15 U.S.C. § 1012. Agreeing with the policy in the Act, this Court then held in *Wilburn Boat Company v. Fireman's Fund Insurance Company,* 348 U.S. 310 (1955):

> "We, like Congress, leave the regulation of marine insurance where it has been—with the States."

348 U.S. at 321.

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1. *Wilburn Boat Company v. Fireman's Fund Insurance Company,* 348 U.S. 310, 316 (1955).

2. Merchant Marine Act of 1920, 41 Stat. 1000, 46 U.S.C. § 885 (a)(2).

3. 15 U.S.C. §§ 1011-12 (1945). The Act was passed in response to this Court's decision in *United States v. South-Eastern Underwriters Assoc.,* 322 U.S. 533 (1944).

Against this legal background, the court of appeals was presented with a Texas shipowner's action against a marine insurer on a hull insurance policy issued to the shipowner in Texas. The insurer was found by the district court to have violated the Texas Insurance Code which allows the insured to recover treble damages and attorney's fees against an insurer engaging in unfair claims settlement practices.[4] The district court's holding was based on the decisions from the highest state court in Texas which have uniformly awarded treble damages against insurers engaging in unfair claims settlement practices.[5] Without citing any of the decisions of the Texas Supreme Court, the court of appeals refused to apply the Texas Statute for a reason not enumerated in the Statute and not enunciated by the state's highest court. Despite the fact that the Texas Supreme Court has granted a treble demage recovery against a property insurer in *Royal Globe v. Bar Consultants,* 577 S.W.2d 688 (Tex. 1979), the court of appeals created[6] an exception

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4. *See* Tex. Ins. Code Ann. Art. 21.21 § 16 (Vernon 1981), App. D.

5. *Royal Globe Insurance Company v. Bar Consultants, Inc.,* 577 S.W.2d 688 (Tex. 1979); *Mayo v. John Hancock Mutual Life Insurance Company of Boston, Mass.,* 711 S.W.2d 5 (Tex. 1986).

6. The district court's award of treble damages was based on two independent and alternative grounds. The first was Lexington's violation of Tex. Ins. Code Ann. Art. 21.21 § 16 and Tex. Ins. Board Order 41060 (App. D) as permitted by the Texas Supreme Court in *Royal Globe v. Bar Consultants, Inc.,* 577 S.W.2d 688, 691 (Tex. 1979) and again held actionable by the Texas Supreme Court in *Mayo v. John Hancock Mutual Life Insurance Company of Boston, Mass.,* 711 S.W.2d 5 (Tex. 1986). The second was for Lexington's violation of Tex. Ins. Code Ann. Art. 21.21 § 16 and Tex. Ins. Board Order 27085 (App. D) (a disputed issue in the Texas intermediate appellate courts). The court of appeals chose to reverse the district court's treble damage award on the second point even though there was an independent alternative ground to affirm the district court which was not attacked by Lexington.

for a marine property insurer, denying recovery for the insurer's unfair claims settlement practices found by the district court.

The refusal by the court of appeals to follow the Texas Insurance Code as interpreted by the Texas Supreme Court has created a serious breach in the uniform policy enunciated by this Court and Congress in marine insurance law. If a federal court can pick and choose which state statutes it will apply to marine insurance policies despite the interpretation given the statute by the state's highest court, then federal interference with state insurance law will prevent effective regulation by the states as mandated by Congress. The interference is particularly invasive when an insurer is absolved from the statutory penalties for its conduct violating state law, as the court of appeals held in this case.

II.

In reversing the district court's award of statutory damages recoverable under Texas law, the court of appeals ruled that the marine property insurer, although not exempted from the Texas Insurance Code by the Texas Legislature or Texas Supreme Court, should not be subject to the statutory damages which other insurers writing insurance in Texas must pay when they are found to have engaged in unfair claims settlement practices in violation of the Texas Statute. Before the court of appeals rendered its decision, the Texas Supreme Court granted a Writ of Error to review one of the intermediate appellate court decisions relied on by the court of appeals to reverse the district court. *Chitsey v. National Lloyds Insurance Company*, 698 S.W.2d 766 (Tex. App.—Austin 1985, writ

of error granted) 29 Tex. Sup. Ct. J. 390 (May 28, 1986). Rather than staying its decision or certifying the question to the Texas Supreme Court,[7] the court of appeals reached out to decide the question of state law currently pending resolution before the Texas Supreme Court in a case involving the precise question presented in the case at bar.[8] Petitioners submit that this action violates fundamental principles of federalism as dictated by the United States Constitution, the McCarran Act and the decisions of this Honorable Court. Further, the court of appeals has disrupted the development of state law by denying the state's highest court the opportunity to resolve the conflicting authorities from its intermediate appellate courts, particularly since that state's highest court is currently reviewing the precise issue at bar.

"A proper respect for state functions" has caused this Honorable Court to recognize that "the National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways." *Younger v. Harris,* 401 U.S. 37, 44 (1971). The same principle is embodied in the Ninth and Tenth Amendments to the United States Constitution,[9] establishing the essence of our federal system of government.

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7. Texas Constitution Art. V § 3-c(a) Vernon Ann. Tex. Const. (1986).

8. *Chitsey v. National Lloyds Insurance Company,* 698 S.W.2d 766 (Tex. App.—Austin 1985, Writ of Error granted), 29 Tex. Sup. Ct. J. 390 (May 28, 1986), was cited by Lexington and the court of appeals for the proposition that Texas law does not provide a private cause of action for treble damages under Art. 21.21 § 16 for unfair claim settlement practices.

9. Amendment IX of the Constitution of the United States in pertinent part provides: "The enumeration in the Constitution of certain rights shall not be construed to deny or disparage others retained by the people." Amendment X of the Constitution of the

Nowhere is the importance of federalism felt more strongly than in the area of insurance law where Congress and this Court have expressly provided that "the continued regulation and taxation by the several states of the business of insurance is in the public interest. . . ." 15 U.S.C. § 1011; *Wilburn Boat v. Fireman's Fund Insurance Co.*, 348 U.S. 310, 319 (1955).

This admiralty case presents the precise situation addressed by this Honorable Court in *Railroad Commission of Texas v. Pullman Company*, 312 U.S. 496 (1941), in which the Court stated that the last word on the interpretition of the Texas statute "belongs neither to us nor to the district court but to the Supreme Court of Texas." 312 U.S. at 500. The court of appeals rendered a decision which is contrary to two decisions of the Texas Supreme Court on the subject, neither of which was cited by the court of appeals.[10] Rather, it was based on an intermediate appellate court's opinion which the Texas Supreme Court is currently reviewing.[11]

United States in pertinent part provides: "The powers not delegated to the United States by the Constitution nor prohibited by it to the states, are reserved to the states respectively or to the people."

10. *Royal Globe Insurance Company v. Bar Consulants, Inc.*, 577 S.W.2d 688 (Tex. 1979), wherein the Texas Supreme Court permitted the recovery of treble damages under Art. 21.21 § 16 against a property insurer for violations of Tex. Ins. Board Order 18663. Board Order 18663 which was at issue in that case involved the identical violation as the instant action. *Mayo v. John Hancock Mutual Life Insurance Company of Boston, Mass.*, 711 S.W.2d 5 (Tex. 1986), wherein the Texas Supreme Court again held that Art. 21.21 § 16 allows a private cause of action for treble damages against an insurer engaging in unfair practices in the handling of a claim prohibited by the Texas Insurance Board Order rules and regulations.

11. *Chitsey v. National Lloyds Insurance Company*, 698 S.W.2d 766 (Tex. App.—Austin 1985, Writ of Error granted), 29 Tex. Sup. Ct. J. 390 (May 28, 1986).

If the Texas Supreme Court follows its earlier decisions on this issue, to paraphrase the *Pullman* opinion, the "unnecessary ruling" of the court of appeals will be "supplanted by a controlling decision of a state court," and "the reign of law" will be "hardly promoted." *Railroad Commission of Texas v. Pullman Company*, 312 U.S. 496, 500 (1941).

Besides the unconstitutional interference in the development of state law, the attempt to decide questions of state law currently pending resolution before a state's highest court can lead to the embarassment of the federal judicial system as explained by Chief Judge Brown of the court of appeals:

> It has been awkward—and, to some, not a little embarrassing—when our first guess turns out to be wrong and the state court makes the second and last guess by reversing our holding. But more important than possible embarrassment is the frustration for litigants when the rule of law we prescribe turns out to be a ticket for one ride only.[12]

Rather than subjecting the federal courts to the potential embarrassment of wrongly divining state law questions which are pending resolution before the state's highest court, the federal courts should stay this decision until the Texas Supreme Court has developed its state law in an orderly fashion or certify the question to the Texas Supreme Court. Not only does this avoid unnecessary interference with constitutionally protected state law development, but it avoids prejudice to litigants when the incorrect prediction "turns out to be a ticket for one ride only."[13]

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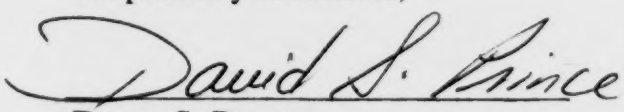
12. Brown, Certification—Federalism in Action, 7 CUMBERLAND L. REV. 455, 456 (1977).

13. *Id.*, 456.

CONCLUSION

The decision of the court of appeals is an affront to the principles of federalism set forth in the United States Constitution, enunciated by this Honorable Court and enacted into law by Congress. Equally important, however, is the impact that the opinion of the court of appeals could have by its unconstitutional interference with the development of insurance law in the State of Texas. For the reasons that are set forth above, Petitioners respectfully pray that this Honorable Court should grant this petition for a writ of certiorari to consider the questions of exceptional importance involved in this appeal.

Respectfully submitted,



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APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 85-2462

OPINION

JIM AUSTIN AND AULEMIC, INC.,
Plaintiffs-Appellees,

v.

SERVAC SHIPPING LINE,
HASSAN A. GAAFAR, IND., AND
LEXINGTON INSURANCE CO.,
Defendants,

LEXINGTON INSURANCE CO.,
Defendant-Appellant.

Filed July 2, 1986

Before: Charles Clark, Chief Judge, E. Grady Jolly and Robert M. Hill, Circuit Judges.

Opinion by Judge Robert M. Hill

Appeal from the United States District Court
for the Eastern District of Texas
Joe J. Fisher, District Judge, Presiding

SUMMARY

Admiralty/Insurance/Damages

Appeal from a district court judgment awarding compensatory, consequential and punitive damages. Affirmed in part, reversed in part and remanded.

Appellee Austin and his wholly owned corporation (collectively Austin) purchased a ship. Thereafter, Austin agreed to a short-term charter party with Servac Shipping Line, Ltd. and its principal (collectively Servac) so that Servac could evaluate the suitability of the ship for its long-term charter needs. Austin obtained a marine hull insurance policy with appellant Lexington Insurance Company (Lexington). During the short-term charter party, the ship suffered mechanical problems and Austin requested coverage from Lexington. Lexington initially rejected the claim, but later undertook a determination of the amount of damages. A year later the parties still could not agree on the cost to repair the ship. Austin filed suit against Lexington, seeking recovery of losses to the ship, lost profits, other consequential damages, and treble damages under the Texas Insurance Code, and also seeking the return of certain layup premiums. The district court entered judgment against Lexington for various damages. On appeal, Lexington offers arguments for reversing the entire judgment, as well as arguments for reducing the amount of damages awarded.

[1] Lexington's first argument for reversal is that alleged misrepresentations made by the insured voided the policy. [2] Lexington claims that Austin's maritime experience was misrepresented. [3] However, the district court's finding that no material misrepresentation occurred is not clearly erroneous. Based on the testimony before it, the court easily could have decided that the correct information was provided but that Lexington's underwriting agent had somehow confused it. [4] Lexington next contends that the policy was void because Austin allowed the ship to sail in an unseaworthy condition. [5] Although the record contains testimony supporting

Lexington's contention that mechanical deficiencies and the incompetence of the crew rendered the ship unseaworthy, it also contains testimony to the opposite effect, the latter amply supporting the district court's finding that the ship was not unseaworthy. [6] As to the cost to repair he ship, the district court selected the figure suggested by Austin's expert; Lexington urges the figure suggested by its expert because he allegedly prepared a more detailed and careful report. However, the credibility judgments Lexington asks on appeal are exactly the judgments that are properly made by the district court. [7] Lexington also argues that applying only one deductible amount to the costs of repairs was error. [8] Because two separate accidents occurred, the district court did err in applying only one deductible, and the recoverable cost of repairs is reduced accordingly. [9] Lexington next attacks the award of layup premiums. The policy provides that the insurance company would return the premiums applicable to each period of thirty consecutive days the vessel was laid up. Although laid up for four consecutive thirty-day periods in Spain, Lexington argues that since it did not approve the layup in Spain, Austin is not entitled to layup premiums. [10] However, the policy is ambiguous as to the necessity of obtaining Lexington's approval, and consequently the ambiguity was properly construed against the insurer. [11] Although Lexington next contends that the district court erred in finding that crew negligence caused the damage to the ship, [12] the expert testimony was conflicting, and the finding that crew negligence caused the damage is entirely plausible. [13] Lexington next argues that the district court erred in finding that its actions caused Austin to suffer the loss of a future, long-term charter party. [14] Although Servac made an offer for a thirty-month charter

of the vessel, no evidence in the record indicates that Austin accepted the offer. Because there are several plausible reasons for Austin's and Servac's failure to agree to a long-term charter party that have nothing to do with Lexington, that element of damages is reversed. [15] Lexington's next contention is that the district court erred in awarding Austin consequential damages for crew wages, port fees, inspections, and other costs incurred while Austin sought repair approval for the ship. [16] While ample evidence indicates that Austin incurred these expenses, no testimony indicates that they would not have been incurred had Lexington promptly determined coverage and paid for the repairs. Thus, this element of the damage award is also reversed. [17] Lexington's final argument is that the district court erred in applying the treble damages provision of the Texas Insurance Code. [18] Since the district court entered judgment, two Texas courts have held that section of the Code did not provide the insured a cause of action for unfair claims settlement practices. [19] Two federal courts sitting in Texas have held the same. Consequently, the district court erred in awarding treble damages under that section of the Code. [20] If Florida rather than Texas law applies to the instant case, the district court would still be in error in awarding the treble damages because Florida law does not permit such a recovery either.

OPINION

ROBERT M. HILL, Circuit Judge:

Defendant Lexington Insurance Company (Lexington) appeals a judgment entered against it following a bench trial. Lexington presents several arguments calling for a

complete reversal and the entry of a take-nothing judgment and several additional alternative arguments calling for a reduction of the damages assessed against it. While we reject the arguments calling for a complete reversal, we accept several of the damage reduction arguments and therefore order the damages reduced accordingly.

I. BACKGROUND

Plaintiffs Jim Austin and his wholly owned corporation, Aulemic, Inc., (collectively Austin) purchased the AMAZON TRADER, a refrigerated freight ship, at a United States Marshal's auction in December 1981 for $125,000. After completing some repair and maintenance work, Austin agreed to a short-term charter party with Servac Shipping Line, Ltd. and its principal, Hassan Gaafar, (collectively Servac) so that Servac could evaluate the suitability of the vessel for its long-term charter needs. Austin obtained a $1,000,000 marine hull insurance policy with Lexington covering the AMAZON TRADER. During the period the policy was in force, pursuant to the short-term charter party, the AMAZON TRADER carried a Servac cargo from Tampa, Florida, to Alexandria, Egypt.

While enroute from Tampa to Alexandria, the ship suffered engine, power train, and generator problems. Austin, through its agent Frank B. Hall & Co. (Hall & Co.), an insurance broker, contacted Lexington about the ship's mechanical problems and requested coverage. Lexington initially rejected the claim as occurring outside the vessel's trading warranty, which included only the Western Hemisphere, but Lexington later undertook a determination of the amount of the damages. One year after the claim arose the parties still could not agree on

the cost to repair the vessel; consequently, Austin brought suit against Lexington, alleging failure to pay claims arising under the policy, seeking recovery of losses covered by the policy, lost profits, other consequential damages, and treble damages under article 21.21 of the Texas Insurance Code, Tex. Ins. Code Ann. art. 21.21 (Vernon 1981), and seeking the return of layup premiums.[1]

The district court, sitting in admiralty without a jury, entered judgment against Lexington in the amount of $367,592 for amounts owed under the policy,[2] plus prejudgment and post-judgment interest, and $2,582,547 in punitive damages[3] under article 21.21, plus costs, post-judgment interest, and stipulated attorney's fees. This appeal followed.

II. LEXINGTON'S CONTENTIONS

Lexington levels numerous attacks on the judgment entered by the district court. Lexington first offers two arguments for reversing the entire judgment: (1) the alleged misrepresentations made by the insured voided the policy, and (2) the alleged unseaworthiness of the vessel voided the policy. Lexington next offers several arguments for reducing the amount of the damages

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1. Austin also sued Servac and Gaafar, alleging breaches of the charter party and seeking actual and consequential damages. The district court entered a take-nothing judgment in favor of Servac and Gaafar. Austin has not appealed the district court's ruling.

2. The amount owed under the policy consisted of the $373,600 cost to repair the vessel, less a $12,500 deductible, plus the return of $6,492 in layup premiums, for a total of $367,592.

3. The punitive damages consisted of the $373,600 cost to repair the vessel, less the $12,500 deductible, plus $390,000 for lost future profits, plus $109,749 of other expenses, for a total of $860,849. The district court then trebled this amount to arrive at a figure of $2,582,547.

awarded against it because the district court erred: (1) in determining the cost to repair the vessel, (2) in subtracting only one deductible amount from the cost to repair, (3) in awarding layup premiums, (4) in determining that crew negligence caused all the losses, (5) in determining that Lexington's actions caused Austin to lose a future charter party agreement, (6) in determining other consequential damages incurred by Austin, and (7) in applying the punitive provisions of article 21.21 of the Texas Insurance Code.

III. LEXINGTON'S LIABILITY

A. *Misrepresentation*

[1] Lexington's first argument for reversal is that the district court erred in finding that the alleged misrepresentations made by the insured did not void the policy.

> Nothing is better established in the law of *marine* insurance than that "a mistake or commission material to a marine risk, whether it be wilful or accidental, or result from mistake, negligence or voluntary ignorance, avoids the policy. And the same rule obtains, even though the insured did not suppose the fact to be material."

Fireman's Fund Insurance Co. v. Wilburn Boat Co., 300 F.2d 631, 646 (5th Cir.), *cert. denied*, 370 U.S. 925, 82 S. Ct. 1562, 8 L.Ed.2d 505 (1962) (emphasis in original) (citation omitted); *see also Gulfstream Cargo, Ltd. v. Reliance Insurance Co.*, 409 F.2d 974, 980 (5th Cir. 1969). "A material fact is any fact, 'the knowledge or ignorance of which would naturally influence an insurer in making the contract at all, or in estimating the degree and character of the risk, or in fixing the rate of insurance.' " 300 F.2d at 640 (citations omitted).

[2] Lexington claims that Hall & Co., Austin's broker, misrepresented Austin's maritime experience by stating that Austin had owned and operated the AMAZON TRADER for twelve years, that Austin owned numerous other maritime interests including twenty fishing vessels, and that Austin was contemplating the purchase of two new vessels, when in fact Austin had just purchased the AMAZON TRADER, had previously owned only one other vessel, an oilfield supply boat, and was not contemplating the purchase of additional vessels. Lexington further claims that the alleged misrepresentations were material to its determination of the risk.

Lexington cites the testimony of one witness, Niels Aaskov, an employee of Lexington's underwriting agent, Southeastern Risk Specialists, to support its contentions. Aaskov testified, based on a worksheet prepared at the time, that an employee of Hall & Co., Frank Sioli, informed him that the owner of the AMAZON TRADER had owned and operated the vessel for twelve years, that the owner owned numerous other vessels, and that the owner was contemplating the purchase of two other vessels. Later, on cross-examination, Aaskov testified that, in addition to gathering information on the current owner, he also compiled information concerning the previous owner. The previous owner of the vessel, Hines Worbs, had operated the vessel for twelve years, owned numerous other vessels, and was contemplating the purchase of two new vessels.

The district court also had before it the testimony of several other witnesses concerning the alleged misrepresentations. Sioli, the agent who contacted Aaskov concerning coverage for the AMAZON TRADER, testified

that he met with Austin before contacting Aaskov and that he knew Austin owned the vessel. He further testified that he knew that the previous owner had not retained any ownership interest or managerial involvement with the vessel and that nothing in Hall & Co's files reflected that Sioli ever told Aaskov otherwise, Austin also testified that he told Sioli and the president of Hall & Co. that he owned the vessel. Furthermore, Lexington issued the policy to: "Aulemic, Inc. and Mr. James D. Austin, c/o Mr. James D. Austin."

[3] We do not believe the district court's finding that no material misrepresentation occurred is clearly erroneous, *see* Fed. R. Civ. P. 52, as it is "plausible in light of the record viewed in its entirety." *Anderson v. City of Bessemer City*, 470 U.S. ____, 105 S. Ct. 1504, 1512, 84 L.Ed.2d 518, 528 (1985). Based on the testimony before it, the district court easily could have decided that Sioli provided Aaskov with the correct information and that Aaskov somehow confused the past owner's experience with the present owner's experience. Since the district court's finding is plausible, we cannot disturb it.[4]

B. *Seaworthiness*

[4] Lexington next contends that the policy was void from its inception because Austin allowed the vessel to sail in an unseaworthiness condition.

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4. Lexington further contends that the AMAZON TRADER was laid-up without a crew and was not operated under her own power from December 1980 to January 1982 and that Hall & Co. should have disclosed this fact to Lexington. Contrary to Lexington's contention, the evidence reveals that the vessel operated until March 12, 1981, when it was arrested for nonpayment of debt. The deck logs further reveal that the crew remained on board into April 1981. Thus, Lexington bases its contention on an incorrect premise.

> A warranty of seaworthiness by the owner is implied in every hull insurance policy unless expressly waived. The warranty is a continuing obligation that "the owner, from bad faith or neglect, will not knowingly permit the vessel to break ground in an unseaworthiness condition. . . . The consequence of a violation of this 'negative' burden is merely a denial of liability for loss or damage caused proximately by such unseaworthiness."

Insurance Co. of North America v. Board of Commissioners, 733 F.2d 1161, 1165 (5th Cir. 1984) (citations omitted); *see also D.J. McDuffie, Inc. v. Old Reliable Fire Insurance Co.,* 608 F.2d 145, 147 (5th Cir. 1979), *cert. denied,* 449 U.S. 830, 101 S. Ct. 97, 66 L.Ed.2d 35 (1980); *Saskatchewan Government Insurance Office v. Spot Pack, Inc.,* 242 F.2d 385, 388 (5th Cir. 1957). The law presumes that every vessel is seaworthy until the contrary is proved, and the burden of proving unseaworthiness lies with the insurance company. *Hanover Fire Insurance Co. v. Holcombe,* 223 F.2d 844, 845-46 (5th Cir.), *cert. denied,* 350 U.S. 895, 76 S. Ct. 154, 100 L.Ed. 787 (1955).

[5] Lexington contends that the AMAZON TRADER was unseaworthy in two respects: (1) various mechanical deficiencies rendered the vessel unseaworthy and (2) the incompetence of the crew rendered the vessel unseaworthy. Lexington relies on the testimony of two expert witnesses to the effect that the vessel was unseaworthy due both to mechanical deficiencies and crew incompetence; however, the record also contains testimony to the opposite effect. At least five witnesses attested to the seaworthiness of the vessel, and one expert witness testified that the entire crew was competent. Since ample testimony supported

the district court's finding that the vessel was not unseaworthy, the district court's finding is clearly plausible in light of the evidence, and we therefore refuse to set aside its finding. *See* Fed. R. Civ. P. 52; *Anderson v. City of Bessemer City,* 470 U.S. at ____, 105 S. Ct. at 1512, 84 L.Ed.2d at 528; *United States v. United States Gypsum Co.,* 333 U.S. 364, 395, 68 S. Ct. 525, 92 L.Ed. 746, 766 (1948).

IV. AMOUNT OF DAMAGES

A. *Repair Costs*

[6] Lexington contends that the district court erred in determining the cost to repair the vessel. The district court selected the figure suggested by Austin's expert, $373,600, and awarded Austin that amount less the $12,500 deductible. Lexington urges us to reject the figure accepted by the district court and to accept the figure suggested by Lexington's expert, $45,851. Lexington would have us overturn the district court's finding because Lexington's expert allegedly prepared a more "detailed" and "careful" report than did Austin's expert and because Austin's expert's report is "ephemeral in the extreme and inherently suspect." The district court observed both experts at trial and heard each expert's explanation of how he arrived at the figures used in the reports. The credibility judgments Lexington asks us to make are exactly the judgments that the Federal Rules of Civil Procedure leave for the district court to make. Fed. R. Civ. P. 52(a) ("due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses"); *Anderson v. City of Bessemer City,* 470 U.S. at ____, 105 S. Ct. 1504, 84 L.Ed.2d at 518 ("[w]hen findings are based on determinations regarding the credibility of

witnesses, Rule 52 demands even greater deference to the trial court's findings"). We therefore refuse to disturb the district court's factual finding as to the cost to repair the vessel.

B. *Deductible Amount*

[7] In addition to arguing that the district court erred in computing the cost to repair the vessel, Lexington also argues that the district court erred in applying only one deductible amount to the costs of repairs. The policy provides: "[T]here shall be deducted from the aggregate of all claims . . . arising out of each separate accident, the sum of $12,500. . . ." Austin maintains that the district court correctly applied only one deductible because only one accident occurred, i.e., the captain's negligence in operating the vessel. Two decisions of the captain caused the damage to vessel: first, when the clutch began slipping, the captain ordered the clutch welded in the engaged position, resulting in damage to the engine and the power train, second, after discovering that the fuel used in the generators was contaminated, the captain allowed the crew to continue using the contaminated fuel in the generators, resulting in damage to the generators.

Lexington urged the district court and now urges this court to apply a separate deductible to each item of equipment damaged by the captain's negligence. For example, Lexington would apply a separate deductible to each of the generators damaged by the contaminated fuel, although the captain's one act of negligence in ordering the use of contaminated fuel damaged all the generators, and would apply separate deductibles to the engine, the clutch, and the tailshaft, although the captain's one act

of negligence in ordering the clutch welded caused the damage to all three of these items.

[8] While we cannot agree with Lexington's contention that up to ten deductibles should apply to Austin's claim, we do agree that the district court erred in applying only one deductible. The court should have applied the deductible twice since two separate accidents occurred. The first occurred when the captain decided to order the clutch welded, and the second occurred when the captain decided to allow the crew to continue using contaminated fuel in the generators. We therefore modify the recoverable cost of repairs by reducing it an additional $12,500 to $348,600.

C. *Layup Premiums*

[9] Lexington next attacks the district court's award of layup premiums to Austin. The policy provides that the insurance company would return the premiums applicable to each period of thirty consecutive days the vessel was laid up. The AMAZON TRADER was laid up for four consecutive thirty-day periods in Spain when it broke down on its way back to Tampa; however, when Austin requested return of the applicable premiums, Lexington refused to return them. Lexington argues that Austin violated the following provision of the policy: "[I]n no case shall a return for lay-up be allowed when the Vessel is lying . . . in any location not approved by the Underwriters." Lexington argues that since Lexington did not approve the layup in Spain, Austin is not entitled to lay up premiums. We disagree.

[10] The policy does not say that Lexington must first approve a layup port; rather, the policy says that

layup premiums will not be allowed when the vessel is laid up in a location "not approved by the Underwriters." This ambiguous phrase could easily be construed as meaning that Lexington maintained a list of unapproved ports and that the vessel could not be laid up at one of those ports. Applying the time-honored rule that ambiguities in insurance policies are to be construed against the insurer, *Walter v. Marine Office of America,* 537 F.2d 89, 94-95 (5th Cir. 1976), we hold that the district court correctly determined that Austin was entitled to layup premiums.

D. *Crew Negligence*

[11] Returning to its wholesale attack on the factual findings made by the district court, Lexington next contends that the district court erred in finding that crew negligence caused the damage to the AMAZON TRADER. This finding was critical to the district court's award of damages for the cost of repairs because the court relied only on the Inchmaree clause of the insurance policy in awarding damages. The Inchmaree clause covers damage to the vessel caused by the negligence of the master, officers, crew, or pilots. Thus, if the damage to the vessel was not the result of crew negligence, the Inchmaree clause does not provide coverage.

[12] Lexington again urges us to accept the version of the facts as related by its expert rather than the version related by Austin's expert and accepted by the district court. Again we must decline. Austin's expert testified that the captain of the vessel was negligent in ordering the clutch welded into a solid unit and in continuing to operate the generators with contaminated fuel. Thus, the district court's finding that crew negligence caused the dam-

age to the vessel is entirely plausible and must be upheld on appeal.

E. *Future Charter*

[13] Lexington next argues that the district court erred in finding that Lexington's actions caused Austin to suffer $390,000 in damages for the loss of a future charter party. The district court found that, under the proposed thirty-month charter party, Austin would have earned a profit of $13,000 a month, resulting in a $390,000 loss when Servac retracted the offer. Lexington argues that its actions did not cause Servac to retract the offer. We agree.

[14] On July 8, 1982, while the AMAZON TRADER was enroute from Tampa to Alexandria, Servac made an offer for a thirty-month charter of the vessel. No evidence in the record indicates that Austin accepted Servac's offer. In early August, before Servac had any knowledge of Lexington's handling of the claim, Servac decided to have nothing more to do with the AMAZON TRADER. Our review of the evidence indicates that, while there are several plausible reasons for Austin's and Servac's failure to agree to a long-term charter party, i.e., mechanical problems with the vessel, delays in the vessel's return voyage, and disputes over whether Servac or Austin was responsible for repairs, none of the explanations have anything to do with Lexington. Thus, finding ourselves left with a definite and firm conviction that a mistake has been made and finding the district court's finding implausible in light of the evidence, we reverse as to this element of damages.

E. *Other Consequential Damages*

[15] Lexington's next contention is that the district court erred in awarding Austin $109,749 in other consequential damages. The damages consisted of Austin's expenses for crew wages, port fees, inspections, and other costs incurred while Austin sought repair approval for the vessel.

[16] While ample testimony and documentation support the district court's finding that Austin incurred these expenses, the evidence fails to connect the expenses with Lexington's actions. No testimony indicated that Austin would not have incurred these expenses had Lexington promptly determined coverage and paid for the repairs. When substantial evidence does not support a finding of the district court, we may set that finding aside as clearly erroneous. *United States v. Florida,* 482 F.2d 205, 208 (5th Cir. 1973); *Ward v. Hobart Manufacturing Co.,* 450 F.2d 1176, 1182-83 (5th Cir. 1971). Since no evidence was introduced to show that Lexington's conduct caused Austin to incur the expenses, the district court's finding is clearly erroneous, and we reverse this element of the damage award.[5]

F. *Treble Damages*

[17] Lexington's final argument is that the district court erred in concluding that it could apply the treble

5. While Austin did not introduce evidence to connect Lexington to the expenses Austin incurred while the vessel was laid up, some of Austin's testimony is relevant to the inquiry. Jim Austin testified that, had Lexington promptly agreed to pay for the needed repairs, these would have incurred approximately $125,000 in expenses for maintaining the crew and vessel while repairs were being made and for bringing the vessel back across the Atlantic. Thus, Austin, according to its own evidence, incurred less expense by Lexington's delay than would have been incurred had Lexington promptly paid for the repairs.

damages provision or article 21.21 of the Texas Insurance Code, Tex. Ins. Code Ann. art. 21.21 § 16 (Vernon 1981).[6] The district court held that the insurance policy was issued to and was payable to Texas plaintiffs and was

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6. At the time of trial and at the time the alleged unfair settlement practices occurred, the pertinent part of article 21.21 read as follows:

> Sec. 16(a) Any person who has been injured by another's engaging in any of the practices declared in Section 4 of this Article or in rules or regulations lawfully adopted by the Board under this Article to be unfair methods of competition and unfair and deceptive acts or practices in the business of insurance or in any practice defined by Section 17.46 of the Business & Commerce Code, as amended, as an unlawful deceptive trade practice may maintain an action against the company or companies engaging in such acts or practices.
>
> (b) In a suit filed under this section, any plaintiff who prevails many obtain:
>
> (1) three times the amount of actual damages plus court costs and attorney's fees reasonable in relation to the amount of work expended;
>
> (2) an order enjoining such acts or failure to act;
>
> (3) any other relief which the court deems proper.

(Vernon 1981). Between the time of trial and the time the district court entered judgment, the Texas Legislature altered article 21.21 to read as follows:

> Sec. 16. (a) Any person who has sustained actual damages as a result of another's engaging in an act or practice declared in Section 4 of this Article or in rules or regulations lawfully adopted by the Board under this Article to be unfair methods of competition or unfair or deceptive acts or practices in the business of insurance or in any practice defined by Section 17.46 of the Business & Commerce Code, as amended, as an unlawful deceptive trade practice may maintain an action against the person or persons engaging in such acts or practices.
>
> (b) In a suit filed under this section, any plaintiff who prevails may obtain:
>
> (1) the amount of actual damages plus court costs and reasonable and necessary attorneys' fees. If the trier of fact finds that the defendant knowingly committed the acts complained of, the court shall award, in addition, two times the amount of actual damages; or
>
> (2) an order enjoining such acts or failure to act; or
>
> (3) any other relief which the court deems proper.

(Vernon Supp. 1986).

therefore subject to the provisions of the Texas Insurance Code. *See* Tex. Ins. Code Ann. art. 21.42 (Vernon 1981). Lexington argues, first, that the court should have applied a federal rule to answer the question of whether treble damages are available and, second, that, if state law does apply, the court should have applied Florida rather than Texas law. Austin maintains that Texas law applies.

We begin our choice of law analysis with *Wilburn Boat Co. v. Fireman's Fund Insurance Co.*, 348 U.S. 310, 75 S. Ct. 368, 99 L.Ed. 337 (1955). *Wilburn Boat* teaches that, in the absence of a controlling federal admiralty rule, we are to turn to state law. *Id.* at 314-16, 99 L.Ed. at 342-44. *Wilburn Boat,* however, does not address the question of which state's law to apply.

Applying *Wilburn Boat,* we turn to the question of whether a controlling federal admiralty rule answers the question raised by the district court's award of treble damages. The question raised is whether, when an insurance company "engage[s] in unfair and deceptive acts or practices" in the handling of its claims, may a district court award the insured three times his damages. Our review of admiralty law has not revealed, nor have the parties cited, any federal rule controlling the damages recoverable by an insured allegedly injured by the insurer's unfair acts in the handling of a claim.[7] In the absence of a controlling federal rule, we must turn to

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7. While Lexington now claims that such a rule exists, Lexington is unable to cite a single case containing a federal rule on the subject. Interestingly, Lexington's Proposed Conclusions of Law filed in the district court contain the following statement: "Any question of unfair or inequitable claims handling is a matter of state law, there being no clearly established rule of federal jurisprudence on the subject."

state law for the answer to the question of whether an insured may recover treble damages for unfair claims handling practices.

Lexington strongly urges the application of Florida law to the case, while Austin maintains that Texas law applies. We find it unnecessary to determine whether Texas or Florida law applies, since the result is the same under each state's law. Neither Texas nor Florida permits the recovery of treble damages under the facts of the instant case.

[18] At the time the district court concluded that article 21.21 permitted Austin to recover treble damages, no Texas court had decided whether article 21.21 applied to a property insurer who failed to fairly handle a claim made by his insured. However, since the district court entered judgment, two Texas Courts of Appeal have addressed situations identical to those in the present case. In both cases the plaintiff-insured alleged that the defendant-insurer engaged in unfair claims settlement practices, and in both cases the Texas courts held that article 21.21 did not provide the insured a cause of action for unfair claims settlement practices.

In *Texas Farm Bureau Mutual Insurance Co. v. Vail,* 695 S.W.2d 692 (Tex. App.—Dallas 1985, no writ) following the insurance company's denial of the insureds' fire loss claim, the insureds recovered treble damages based on their allegations of unfair claims settlement practices. The court of appeals, in holding that article 21.21 did not permit the insured to recover damages, stated that " 'it was the intent of the legislature to "seal off" unfair claims settlements from the expansive language of the DTPA and the Insurance Code.' " *Id.* at

694 (citation omitted). In *Chitsey v. National Lloyd's Insurance Co.*, 698 S.W.2d 766 (Tex. App.—Austin 1985, writ of error granted), the jury found, in answer to a special issue, that the insurer engaged in an unfair act or practice in its handling of the insured's claim. The court of appeals held that the jury's finding did not entitle the insured to recover treble damages because article 21.21 did not apply to unfair claims settlement practices.[8]

[19] Two federal district courts sitting in Texas have also held that article 21.21 does not provide the insured a cause of action for unfair claims settlement practices against property insurers. *Lexington Insurance Co. v. Bennet Evans Grain Co.*, No. C.A. G-84-184 (S.D. Tex. Feb. 17, 1986); *South Texas National Bank of Laredo v. United States Fire Insurance Co.*, No. C.A. L-83-34 (S.D. Tex. Jan. 10, 1985). Thus, if Texas law applies to the instant case, the district court erred in awarding treble damages to Austin.

[20] Similarly, Florida law does not provide the insured with a cause of action for treble damages if the insurance company engages in unfair claims settlement

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8. Austin argues that the decisions of the Texas Court of Appeals, rather than reaching consistent decisions on the applicability of section 21.21 to unfair claims settlement cases, are split. Austin cites two cases for this proposition. *Allstate Insurance Co. v. Kelly*, 680 S.W.2d 595 (Tex. App.—Tyler 1984, writ ref'd n.r.e.); *St. Paul Insurance Co. v. McPeak*, 641 S.W.2d 284 (Tex. App.—Houston [14th Dist.] 1982, writ ref'd n.r.e.). As the court in *Vail* noted, the duties and responsibilities of a property insurer differ from those of other types of insurance providers. *Vail*, 695 S.W.2d at 694. In *Kelly* the insured brought suit for the insurer's handling of a suit brought by a third party against the insured. In *McPeak* the insured brought suit after the insurer terminated his worker's compensation benefits. Since *Kelly* and *McPeak* are distinguishable from *Vail* and *Chitsey*, both property cases, the Texas cases addressing unfair claims settlements in a property damage context are consistent.

practices. By statute, Florida law prohibits unfair practices, Fla. Stat. Ann. § 626.9521 (West 1984), and specifically provides that unfair claims practices are one type of unfair practice, Fla. Stat. Ann. § 626.954(i). The section prohibiting unfair practices, section 626.9521, provides that the violator shall be subject to penalties provided in section 627.381, which in turn provides for administrative fines and license suspensions, but does not provide for recovery of treble damages. Fla. Stat. Ann. § 627.381 (West 1984). Thus, if Florida rather than Texas law applies to the instant case, the district court would still be in error in awarding Austin treble damages. Since neither Texas nor Florida law permits the recovery of treble damages from an insurer who engages in unfair claims settlement practices, we reverse the portion of the district court's judgment awarding Austin treble damages.[9]

IV. CONCLUSION

We affirm the portion of the district court's judgment awarding Austin $361,100 as his costs of repairs; however, we modify that amount by subtracting an additional deductible of $12,500, leaving a recoverable cost of repairs of $348,600. We also affirm the portion of the judgment awarding Austin layup premiums in the amount of $6,492. We reverse all the remaining portions of the judgment awarding damages against Lexington. We remand the case to the district court with instructions to enter judgment for Austin in the amount of $355,092,

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9. Lexington also argues that the district court's factual findings regarding Lexington's resolution of Austin's claim are clearly erroneous. In light of our holding that Austin is not entitled to excess damages for unfair claims settlement practices, if any, we need not reach this contention.

plus attorney's fees, costs, and pre-and post-judgment interest.[10]

AFFIRMED IN PART, REVERSED IN PART, AND REMANDED.

10. The district court awarded Austin attorney's fees in amounts stipulated to by the parties. Lexington has not appealed this portion of the district court's judgment; therefore, the district court should include the stipulated amount of attorney's fees for the trial and appeal in the new judgment.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF TEXAS
BEAUMONT DIVISION

CIVIL ACTION NO. B-83-436-CA

JIM AUSTIN and AULEMIC, INC.

v.

SERVAC SHIPPING LINE, LTD.,
HASSAN A. GAAFAR, INDIVIDUALLY
AND LEXINGTON INSURANCE COMPANY

(Filed June 6, 1985)

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MEMORANDUM OPINION

Plaintiffs, JIM AUSTIN and AULEMIC, INC., brought this admiralty suit against LEXINGTON INSURANCE COMPANY to recover for the loss of their vessel, the M/V Amazon Trader, which was insured under an American Institute Time Hull Policy issued by Lexington. Plaintiffs also sought statutory penalties for unfair claims handling practices in violation of TEX. INS. CODE ANN. art. 21.21 (Vernon 1981).

Plaintiffs sued SERVAC SHIPPING LINE, LTD. and HASSAN A. GAAFAR, Individually, to recover for the breach of a charter party for the M/V Amazon Trader. Servac Shipping Line, Ltd. counterclaimed against Jim Austin, individually, for breach of the same agreement.

Both the charter party and insurance policy are maritime contracts within the admiralty jurisdiction of the

Court. Because the charter and insurance contracts were both Texas contracts which were to be performed in whole or in part by the parties in Texas, the Court has *in personam* jurisdiction of the Defendants. Lexington's policy of insurance was issued to and is payable to Plaintiffs in Beaumont, Texas. The policy was, therefore, a Texas contract per Tex. Insur. Code Ann. art. 21.42 (Vernon 1981). The charter party was received and signed by Austin in Beaumont, Texas. Under the charter, Austin paid the monthly mortgage payments on the vessel to the Parkdale Bank in Beaumont. Servac was required to and Gaafar did report to Austin in Beaumont on the vessel's performance and made an offer for a long-term charter. The Court concludes that the Defendants were "doing business" in the state of Texas, within the meaning of art. 2031(b), Tex. Rev. Civ. Stat. Ann. (Vernon 1964 and Supp. 1985).

The parties tried the case to the Court, sitting in admiralty. The Court heard the testimony of nineteen (19) witnesses, both live and by deposition. In addition, all parties submitted extensive pre-trial and post-trial briefs.

After careful review of the evidence, the Court finds and concludes that at all material times prior to June 16, 1982, the M/V Amazon Trader was seaworthy and reasonably fit for its intended use; that the damage to the vessel was caused by the negligence of the master and crew, which peril was insured under the insurance policy; and that Lexington Insurance Company has engaged in "unfair and deceptive acts or practices" in the handling of Plaintiffs' claims in violation of TEX. INS. CODE ANN. art. 21.21. Consequently, judgment will be

entered for Plaintiffs against Lexington Insurance Company.

The Court further concludes that Plaintiffs should take nothing by reason of their suit against Servac Shipping Line, Ltd. and Hassan A. Gaafar, and that Servac Shipping Line, Ltd. take nothing by reason of its counterclaim against Jim Austin.

A. THE VESSEL

Jim Austin is the sole owner of Aulemic, Inc., a Cayman corporation having its principal place of business in Beaumont, Texas. Aulemic, Inc. bought the M/V Amazon Trader in December 1981. Aulemic had the vessel surveyed and refurbished, spending in excess of $200,000 to make it fit for transoceanic refrigerated cargo voyages. Extensive surveys by at least three marine surveyors found the vessel fit for duty and it was so certified. Among other things, the surveyors inspected certain of the devices which later failed at sea from misuse.

B. THE CHARTER PARTY

In early May 1982, Hassan Gaafar, President of Servac, contacted Austin at his residence in Beaumont, Texas for the purpose of chartering the vessel to carry frozen cargo to Alexandria, Egypt from Tampa, Florida. Austin and Gaafar agreed to enter into a charter party and on June 2, 1982, Austin, on behalf of Aulemic, received and signed in Beaumont a charter party with Servac. Performance of the parties' obligations under the charter agreement was guaranteed by both Austin and Gaafar in their individual capacities.

In that charter party, Austin did not charge a freight rate or hire for use of the vessel. Instead, Austin entered the charter party so Servac could evaluate the vessel in anticipation of entering into a long-term charter. Under the charter party, Servac agreed to pay all expenses of the vessel during the charter from June 1st until the vessel returned to Tampa.

C. THE INSURANCE POLICY

Plaintiffs' insurance broker, Frank B. Hall & Co. of Florida, placed hull insurance on the Amazon Trader on February 10, 1982 with Lexington Insurance Company. Lexington's policy of marine insurance was issued to Plaintiffs in Texas on July 1, 1982. Lexington insured Plaintiffs' vessel in the amount of $1,000,000 against loss and damage for the period from February 10, 1982 to February 10, 1983. Lexington had been instructed to name James D. Austin, the principal of Aulemic, Inc., as an additional insured and Parkdale Bank of Beaumont as mortgagee.

D. THE VOYAGE

On June 13, 1982, the Amazon Trader sailed from Tampa, with a master and crew hired by Austin, on a round-trip voyage to Alexandria, Egypt carrying the cargo of Servac: many tons of frozen turkeys. The captain, David Ashbee, was qualified to serve as master of the vessel. His nine crewmen were qualified in their jobs and the Amazon Trader was properly manned, equipped and supplied and reasonably fit for the voyage to Alexandria, Egypt.

Thrre days out of Tampa the captain stopped the vessel's engine to repair a slipping clutch. The vessel was then located approximately 70 to 80 miles off the east coast of Florida and within its trading warranty. The chief engineer gave the Captain two options: Either call a seatug to take her back to port for proper repairs, or weld the clutch into a solid unit.

Captain Ashbee made a serious error in judgment by ordering the chief engineer to weld the clutch into a solid unit without first consulting the owner. The welding of the clutch caused a misalignment of the vessel's main engine power train. The continued operation of the vessel in that condition resulted in extensive damage to the vessel's main engine, clutch, thrust-bearing and tail-shaft. In addition to the mechanical problems noted above, the vessel suffered a fire and its generators were damaged by contaminated fuel.

Ashbee knew the repairs to the clutch were temporary and that the chief engineer recommended proper repairs in the next available port. But he continued on to Alexandria because the Charterer's agent advised him "to continue to Egypt and in Egypt we'd have all the major repairs corrected when you discharge the cargo." Moreover, Gaafar gave Ashbee an arrival deadline before the vessel left Florida. The vessel arrived in Alexandria on July 15 and discharged its cargo.

Prior to the vessel's arrival in Alexandria, Plaintiffs received, in Beaumont, Servac's favorable evaluation of the vessel's performance and an offer for a long-term 30 month charter. Under this proposed charter party, Plaintiffs were to realize at least $13,000 a month clear net profit for the 30 months of the charter, resulting in

at least $390,000 profit from the long-term charter of the vessel to Servac.

Before addressing the dispute with Lexington, the Court will dispose of the cross claims of Austin and Gaafar and of their companies. Both Austin and Gaafar allege breaches of their charter party agreement by the other's company. The Court concludes that it was the intention of the parties that Servac pay all expenses, including repairs to the vessel, incurred in shipping its product to Egypt. That was simply the consideration for using the vessel.

Because Servac actually paid the expenses of the vessel during the charter, the Court concludes that Gaafar and Servac did not breach the charter party.

Servac's allegations that Plaintiffs failed to exercise due diligence and breached the implied warranty of seaworthiness are without merit. The damages Servac seeks from Austin in its counterclaim, by the admission of Servac's President, Gaafar, are either related to an earlier charter party for which Servac indemnified Aulemic or are expenses incurred in operating the vessel.

Maritime law permits parties to assume liabilities in contracts as they choose. *J.B. Effenson Co. v. Three Bays Corporation, Ltd.*, 238 F.2d 611 (5th Cir. 1956). The Court concludes that Servac's position is contrary to the plain reading of the contract and to Servac's earlier course of action. Accordingly, the Court holds there was no breach by Austin.

E. THE DAMAGE CLAIMS AND DENIALS

The balance of the lawsuit concerns the refusals of Lexington to pay claims under the marine insurance

policy and its liability to Austin for its failure to pay claims.

1. THE AUGUST 1982 DAMAGE CLAIM AND DENIAL

On August 3, 1982, Austin reported to Frank B. Hall & Co. two claims for main engine damage and a fire which occurred on the vessel while en route from Florida to Egypt. Frank B. Hall & Co. immediately notified Lexington of the two claims under the policy. The policy contained a trading warranty which insured the vessel only while within the Western Hemisphere. Lexington refused to pay, insisting that Aulemic breached that warranty and thereby voided the coverage.

The Court finds that all the damage to the Amazon Trader occurred in the Western Hemisphere and within the vessel's trading warranty. The Court further finds that Lexington failed to conduct a reasonable investigation under the circumstances and summarily denied both claims on August 4, 1982. Frank B. Hall & Co. advised Lexington on August 5, 1982 that the main engine damage occurred within the vessel's trading warranty, as stated in the policy, but Lexington continued to deny coverage and closed both claims files on August 23, 1982.

Among other perils insured by Lexington in the policy were those contained in the "Inchmaree" clause, which provides in part: "Subject to the conditions of this policy, this insurance also covers loss of or damage to the vessel directly caused by the following: Negligence of Masters, Officers, Crew or Pilots, provided such loss or damage has not resulted from want of due diligence by the Assured, the Owners or Managers of the vessel,

or any of them." The Court finds and concludes that the damage to the Amazon Trader fell within the Inchmaree Clause of the insurance policy issued by Lexington.

2. THE OCTOBER 1982 DAMAGE CLAIM AND DENIAL

While in port in Alexandria, the Amazon Trader underwent repairs to a rear shaft bearing. Captain Ashbee knew the repairs were only temporary and that the vessel required major repairs to the main engine, clutch, thrust-bearing, tail-shaft and generators. In September, 1982, the vessel was moved to Malaga, Spain for complete repairs. Frank B. Hall & Co. again notified Lexington of Plaintiffs' claims. In October, 1982, Austin inspected the vessel with the owners of two similar vessels. The vessel owners estimated the reasonable cost of repairs to be $400,000. Frank B. Hall & Co. made demand in that amount on Lexington. Lexington continued to deny Plaintiffs' claims and failed to provide Plaintiffs a reasonable explanation of the basis in the policy, in law, or in fact for the denial of the claims.

3. THE FEBRUARY 1983 SURVEY AND DENIAL

In January, 1983, Plaintiffs employed a marine surveyor, Percy Overman, to conduct a damage survey. In his damage survey report, Overman concluded that the reasonable cost of repairs to the Amazon Trader was $373,600. Lexington's surveyor from the Salvage Association, John Riley, initially agreed the damage was caused by crew negligence and so stated in his survey report dated February 9, 1983. Despite this information, Lexington continued to deny Plaintiffs' claims and refused to approve a shipyard for repairs. In late February, 1983,

Lexington was advised that because Plaintiffs' claims were being denied, Plaintiffs would be forced to sell the vessel in its distressed condition. Plaintiffs sold the Amazon Trader, unrepaired, on April 12, 1983 for $30,000 in mitigation of their damage.

As a result of Lexington's failure to conduct a reasonable investigation and to properly and fairly handle the claims, Plaintiffs incurred $109,748.88 in expense for crew wages, port expenses, agents, inspections and costs while seeking repair approval from Lexington and prior to the sale of the vessel. In addition, Plaintiffs sustained $390,000 lost profits on the long-term 30 month charter of the vessel to Servac. The Court finds that Plaintiffs would have earned these profits, had Lexington authorized and paid for the necessary repairs on a timely basis.

F. COVERAGE UNDER THE POLICY

Lexington denies coverage of the Amazon Trader, claiming the vessel was unseaworthy at the attachment of the policy and upon its departure from Key West and Tampa because Plaintiffs failed to exercise due diligence to prepare the vessel; because the master and crew were unqualified; and because Plaintiffs misrepresented the nature of the risk insured.

The law presumes that every vessel is seaworthy until the contrary is proved, and the burden of proving that a vessel is unseaworthy lies upon the insurance company. *Hanover Fire Insurance Company v. Holcombe,* 233 F.2d 844 (5th Cir. 1955).

A shipowner's obligation under a hull policy is extremely limited. The vessel must be seaworthy at the attachment of the insurance, but henceforth, the sea-

worthiness obligation is a sort of negative warranty, i.e. the owner or those in privity with him must not fail to exercise due diligence and send the vessel to sea in a deficient condition. *Tropical Marine Products, Inc. v. Burmingham Fire Insurance Company,* 247 F.2d 116 (5th Cir. 1957), *cert. denied,* 355 U.S. 903 (1957).

A shipowner's warranty of seaworthiness is not that a vessel shall continue absolutely to be kept in a seaworthy condition, or even that she be so at the inception of each voyage or before departure from each port during the policy term. *Saskatchewan Government Insurance Office v. Spotpack, Inc.,* 242 F.2d 385 (5th Cir. 1957).

Although the Inchmaree Clause of a hull policy refers to "due diligence" of the owner to keep the vessel seaworthy, it was not intended as a restriction of coverage, but was intended to broaden coverage in response to the practical business needs of the shipping world in the face of adverse court decisions. *Id.* at 391. *Tropical Marine Products, Inc. v. Burmingham Fire Insurance Company,* 247 F.2d at 122 (5th Cir. 1957). An Inchmaree Clause does in fact underwrite unseaworthiness of many types, such as that occasioned by the negligence of the master or that resulting from a latent defect in hull or machinery. *Id.* at 123.

The Court concludes that Plaintiffs exercised due diligence and that the Amazon Trader was in a seaworthy condition and reasonable fit for its intended use at all material times prior to June 16, 1982. The vessel was properly manned with a qualified master and crew. Contrary to Lexington's allegation that the nature of the risk was misrepresented, the Court concludes that Lexington knew who and what it was insuring. Lexington has failed

to sustain its burden on any contention to vitiate coverage. The Court finds therefore that the policy was in effect and provided coverage for the loss under the Inchmaree Clause. The damage to the Amazon Trader occurred in the Western Hemisphere and within the vessel's trading warranty. Plaintiffs are entitled to recover for all damage sustained by the vessel as a result of the master's and crew's negligence.

G. APPLICATION OF TEXAS LAW

The Supreme Court has ruled that state law should be applied in the field of marine insurance, at least where entrenched Federal precedent is lacking, with respect to a specific issue. *Wilburn Boat Company v. Fireman's Fund Insurance Company,* 348 U.S. 310 (1962). As a Texas contract, the insurance policy is governed by Texas law, including all pertinent provisions of the Texas Insurance Code. Article 21.21, sec. 16 of the Code provides that a cause of action for treble damages may be brought by any person who has been "injured" by another's acts and conduct amounting to "unfair and deceptive acts or practices" in the business of insurance as declared in the lawfully promulgated rules and regulations of the State Board of Insurance. *Royal Globe Insurance Co. v. Bar Consultants,* 577 S.W.2d 688 (Tex. 1979).

Plaintiffs sought relief under Sec. 16 of art. 21.21 for violations of Insurance Board Order 41060 Sec. .003 and .003(b) and argued that Lexington "engaged in unfair and deceptive acts or practices" in the handling of its claims, in violation of Sec. 3(i) and 3(o) of Insurance Board Order 27085. Plaintiffs also argued that Lexington violated Insurance Board Order 41060 Sec. .004(4).

The Texas State Board of Insurance previously adopted Board orders which prohibited, *inter alia,* misrepresentation of an insurance policy and unfair claim settlement practices, the latter including failure to reasonably explain a claim's denial and refusal to pay claims absent a reasonable investigation. Board Orders 41060 (July 22, 1982), 27085 (May 17, 1974).

The Court concludes that Lexington has violated Insurance Board Order 41060 Sec. .003 by committing "unfair and deceptive acts or practices" in violation of Sec. 3(i) and 3(o) of Insurance Board Order 27085. Lexington's wrongful denial of Plaintiffs' claims on August 4, 1982 and thereafter was based its failure to conduct a reasonable investigation. Lexington knew or could have learned that the loss occurred in the Western Hemisphere and within the confines of the vessel's trading warranty, yet persistently insisted there had been a breach of that warranty which voided coverage. Lexington has also violated Insurance Board Order 41060 Sec. .003 by its misrepresentation of the insurance policy, which amounts to "unfair and deceptive acts or practices" in the business of insurance. The Court further concludes that Lexington has violated Insurance Board Order 41060 Sec. .004(4). Plaintiffs have been "injured" by Lexington's egregious conduct and are entitled to recover damages resulting from Lexington's violations of art. 21.21 Sec. 16 and the above-noted rules and regulations of the Texas State Board of Insurance.

Having determined that there was coverage for the loss and that Lexington has violated TEX. INS. CODE ANN. art. 21.21, the Court must now ascertain Plaintiffs' damages. It was undisputed that if repairs had been carried out in Malaga, Spain on the Amazon Trader, the sound

market value of the vessel would have been $480,000. The vessel was sold unrepaired for $30,000 less Plaintiffs' survey cost of $9,578 resulting in a depreciation in value of $459,758. The testimony of Plaintiffs' surveyor, Percy Overman, established the reasonable value of repairs was $373,600. The Court concludes that Plaintiffs are entitled to recover $373,600 minus policy deductible of $12,500, for a total of $361,100. Plaintiffs are also entitled to the return of unearned layup premiums of $6,492 for the four consecutive 30 day periods the vessel was in Malaga not under repair. Plaintiffs are therefore entitled to recover the sum of $367,592 under the policy, with prejudgment interest on this sum from the date of the denial of Plaintiffs' loss, August 4, 1982.

Plaintiffs' actual damages caused by Lexington's violations of TEX. INS. CODE ANN. art. 21.21, however, go beyond the mere costs of repairing the vessel, owed under the policy. As a direct result of Lexington's "unfair and deceptive acts or practices" in the handling of their claims, Plaintiffs incurred $109,749 in expenses for crew wages, port expenses, agents, inspections and costs while seeking repair approval and in the sale of the vessel. Moreover, Plaintiffs undisputably lost $390,000 by being unable to contract for the long-term charter of the vessel to Servac. That loss of profit was proximately caused by Lexington's violations of Article 21.21. To the above amounts must be added the costs of repair payable under the policy: $361,100.

The Court finds that Plaintiffs' actual damages caused by Lexington's violations of the Insurance Code total $860,849. Plaintiffs are entitled to receive, the Court concludes, punitive damages three times that amount:

$2,582,547. Plaintiffs may also recover reasonable attorneys' fees and costs of court.

CONCLUSION

In summary, the Court concludes that there was coverage under the policy for the damage to Plaintiffs' vessel and that Plaintiffs are entitled to recover the reasonable cost of repairs and statutory penalties caused by Lexington's violation of TEX. INS. CODE ANN. art. 21.21. It is therefore

ORDERED, ADJUDGED and DECREED that judgment be entered for Plaintiffs, JIM AUSTIN and AULEMIC, INC., against Defendant, LEXINGTON INSURANCE COMPANY, in the sum of $367,592 for amounts owed under the insurance policy, plus prejudgment interest of ten percent (10%) of said sum, accruing from August 4, 1982; and $2,582,547 in punitive damages for Lexington's violations of TEX. INS. CODE ANN. art. 21.21. Plaintiffs shall also recover reasonable attorney's fees and costs of court. The parties will be expected to stipulate the amount of attorney's fees, but not that said attorney's fees are recoverable, and advise the Court within fifteen (15) days from the date of entering of this Memorandum Opinion. If the parties cannot agree, the Court will determine the amount. Interest on the judgment shall accrue at the rate of 9.15% from this date until paid in full.

It is further ORDERED, ADJUDGED and DECREED that Plaintiffs JIM AUSTIN and AULEMIC, INC. recover nothing against the Defendants, HASSAN A. GAAFAR, individually, and SERVAC SHIPPING LINE, LTD., and that Defendant SERVAC SHIPPING LINE,

LTD. recover nothing against Plaintiff JIM AUSTIN, individually.

SIGNED AND ENTERED this the 6th day of June, 1985.

/s/ JOE J. FISHER
United States District Judge

APPENDIX C

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 85-2462

JIM AUSTIN and AULMIC, INC.,
Plaintiffs-Appellees,

v.

SERVAC SHIPPING LINE,
HASSAN A. GAAFAR, IND.,
and LEXINGTON INSURANCE CO.,
Defendants,

LEXINGTON INSURANCE CO.,
Defendant-Appellant.

Appeal from the United States District Court
for the Eastern District of Texas

ON PETITION FOR REHEARING AND
SUGGESTION FOR REHEARING EN BANC

(Opinion April 8, 5 Cir., 1986, ___F.2d___)

(August 4, 1986)

Before CLARK, Chief Judge, JOLLY and HILL, Circuit Judges.

PER CURIAM:

Appellees' Petition for Rehearing is DENIED and no member of this panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc, (Federal Rules of Appellate Procedure and Local Rule 35) the Suggestion for Rehearing En Banc is DENIED.

* * *

ENTERED FOR THE COURT:

/s/ R. M. HILL
United States Circuit Judge

APPENDIX D

TEXAS INSURANCE CODE

ARTICLE 21.21

* * *

Relief available to injured parties

Sec. 16. (a) Any person who has been injured by another's engaging in any of the practices declared in Section 4 of this Article or in rules or regulations lawfully adopted by the Board under this Article to be unfair methods of competition and unfair and deceptive acts or practices in the business of insurance or in any practice defined by Section 17.46 of the Business & Commerce Code, as amended, as an unlawful deceptive trade practice may maintain an action against the company or companies engaging in such acts or practices.

(b) In a suit filed under this section, any plaintiff who prevails may obtain:

(1) three times the amount of actual damages plus court costs and attorneys' fees reasonable in relation to the amount of work expended;

(2) an order enjoining such acts or failure to act;

(3) any other relief which the court deems proper.

(c) On a finding by the court that an action under this section was groundless and brought in bad faith or for the purpose of harassment, the court may award to the defendant reasonable attorneys' fees in relation to the amount of work expended.

(d) In an action under this section, damages may not include any damages incurred beyond a point two years prior to the institution of the action.

* * *

STATE BOARD OF INSURANCE
STATE OF TEXAS

(S E A L)

IT IS HEREBY CERTIFIED That the instrument which is hereunto attached is a true, full and correct copy of Official Order No. 27085 of the State Board of Insurance of the State of Texas, dated May 17, 1974, consisting of six (6) pages; Subject Considered:

REGULATION IN RESPECT OF UNFAIR CLAIM SETTLEMENT PRACTICES

now on file in and forming a part of the records of the State Board of Insurance.

IN WITNESS WHEREOF, I hereunto subscribe my name and affix the Seal of the State Board of Insurance, in the City of Austin, State of Texas this

15th day of July, 1981

EULA E. (PAT) WAGNER
Chief Clerk

By: /s/ LADELL ANDERSON
Asst. Chief Clerk

No. 27085

RECORD OF OFFICIAL ACTION
of the
STATE BOARD OF INSURANCE
AUSTIN, TEXAS

Date May 17, 1974

Subject Considered:

REGULATION IN RESPECT OF UNFAIR CLAIM SETTLEMENT PRACTICES

General remarks and official action taken:

On January 31, 1974, the State Board of Insurance, after notice, held a public hearing on unfair claim settlement practices rules. Based upon the necessity shown in such hearing for the issuance of rules and regulations pertaining to unfair claim settlement practices, the State Board of Insurance does hereby, under the provisions of Article 21.21-2 of the Insurance Code, promulgate the following rules and regulations pertaining to unfair claim settlement practices:

RULES AND REGULATIONS OF THE STATE BOARD OF INSURANCE IN RESPECT OF UNFAIR CLAIM SETTLEMENT PRACTICES

Section 1. SHORT TITLE.

These regulations shall be known as the "Unfair Claim Settlement Practices Rules."

Section 2. DEFINITIONS.

The following words or phrases as used in these regulations shall have the meaning placed opposite them unless the explicit wording of a regulation shall otherwise direct:

(a) Claim—A request or demand reduced to writing and filed by a Texas resident with an insurer for payment of funds or the providing of services under the terms of a policy, certificate or binder of insurance.

(b) Claimant—A person making or having made a claim.

(c) Complaint—Any written communication, not solicited by an insurer, primarily expressing a grievance relating to an unfair claim settlement practice as defined in Section 3 hereof.

(d) First party coverage—Benefits and other rights provided by an insurance contract to an insured.

(e) Third party coverage—Benefits and other rights provided by an insurance contract to any person other than an insured.

(f) Insurer—Any person, or persons acting in concert, doing or licensed to do business in Texas under Subchapter G of Chapter 3 or Subchapters A, B or C of Chapter 5 of the Insurance Code, as amended, and including (when applicable) proprietorships, partnerships, corporations and unincorporated associations, stock and mutual life, health, accident, fire, casualty, fire and casualty, hail, storm, title, and mortgage guarantee companies; mutual assessment companies; local mutual aid associations; local mutual burial associations; statewide mutual assessment

companies; stipulated premium companies; fraternal benefit societies; group hospital service organizations; county mutual insurance companies; Lloyds; reciprocal or inter-insurance exchanges and farm mutual insurance companies when transacting such business.

(g) Policyholder—The owner of a policy, certificate, or binder of insurance, and any insured, named insured, or obligee under a bond.

Section 3. UNFAIR CLAIM SETTLEMENT PRACTICES.

No insurer shall engage in unfair claim settlement practices. Unfair claim settlement practices shall mean committing or performing with such frequency as to indicate a general business practice any of the following:

(a) Misrepresenting to claimants pertinent facts or policy provisions relating to coverages at issue.

(b) Failing to acknowledge with reasonable promptness pertinent communications with respect to claims arising under its policies, provided that "pertinent communications" shall exclude written communications that are direct responses to specific inquiries made by the insurer after initial report of a claim. An acknowledgement within 15 working days shall be presumed reasonably prompt.

(c) Failing to adopt and implement reasonable standards for prompt investigation of claims arising under its policies.

(d) Not attempting in good faith to effectuate prompt, fair, and equitable settlements of claims submitted in which liability has become reasonable clear.

(e) Compelling policyholders to institute suits to recover amounts due under its policies by offering substantially less than the amounts ultimately recovered in suits brought by them.

(f) Failure of any insurer to maintain a complete record of all complaints which it has received during the preceding three years or since the date of its last examination by the Commissioner of Insurance, whichever time is shorter. This record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of these complaints, and the time it took to process each complaint. A record of such complaints maintained in substantially the form as indicated on Exhibit A attached hereto will be presumed to be in compliance with this requirement, but Exhibit A shall not be considered as the exclusive method to record such complaints.

(g) Failing to provide promptly, when provided for in the policy, claim forms when the insurer requires such forms as a prerequisite for a claim settlement.

(h) Not attempting in good faith to settle promptly claims where liability has become reasonably clear under one portion of the policy in order to influence settlement under other portions of the policy coverage. (This provision shall not apply to those situations where payment under one portion of coverage constitutes evidence of liability under another portion of coverage.)

(i) Failing to provide promptly a policyholder a reasonable explanation of the basis in the insurance policy in relation to the facts or applicable law for denial of a claim or for the offer of a compromise settlement.

(j) Failing to affirm or deny coverage of a claim to a policyholder within a reasonable time after proof of loss statements have been completed. The taking of a non-waiver agreement or the submission of a reservation of rights letter by an insurer to the policyholder within a reasonable time shall be deemed compliance with the provisions of this paragraph.

(k) Except as may be specifically provided in the policy, to refuse, fail, or unreasonably delay offer of settlement under applicable first-party coverage on the basis that other coverage may be available or third parties are responsible in law for damages suffered.

(l) Attempting to settle a claim for less than the amount to which a reasonable man would have believed he was entitled by reference to written or printed advertising material accompanying or made part of an application.

(m) Undertaking to enforce a full and final release from a policyholder when, in fact, only a partial payment has been made. (This rule shall not prevent or have application to the compromise settlement of doubtful or disputed claims.)

(n) Failing to establish a policy and proper controls to make certain that agents calculate and deliver to policyholders or their assignees funds due under policy provisions relative to cancellation of coverage within a reasonable time after such coverages are terminated.

(o) Refusing to pay claims without conducting a reasonable investigation based upon all available information.

(p) Failing to respond promptly to a request by a claimant for personal contact about or review of the claim.

Section 4. SPECIAL CLAIMS REPORTS AND STATISTICAL PLAN.

If it should be found by the State Board of Insurance, based on complaints of unfair claims settlement practices as described in Section 3 hereof, that an insurer is substantially out of line and should be subjected to closer supervision with respect to such practices, it may require such insurer to file a report at such periodic intervals as the Board deems necessary. For purposes of this Section, the term "substantially out of line" shall mean "a patently disproportionate number of complaints to indicate the existence of a pattern of unfair claim settlement practices as that term is defined in Section 3 hereof." Such periodical reports shall contain the following information:

(a) The total number of written claims filed, including the original amount filed for by the insured and the classification by line of insurance of each individual written claim, for the past 12 month period or from the date of the insurer's last periodic report, whichever time is shorter;

(b) The total number of written claims denied for the past 12 month period or from the date of the insurer's last periodic report, whichever is shorter;

(c) The total number of written claims settled, including the original amount filed for by the insured, the settled amount, and the classification of line of insur-

ance of each individual settled claim, for the past 12 month period or from the date of the insurer's last periodic report, whichever time is shorter;

(d) The total number of written claims for which lawsuits were instituted against the insurer, including the original amount filed for by the insured, the amount of final adjudication, the reason for the lawsuit and the classification by line of insurance of each individual written claim, for the past 12 month period or from the date of the insurer's last periodic report, whichever time is shorter; and

(e) The total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of these complaints, and the time it took to process each complaint. Such periodic reports shall be filed with the State Board of Insurance and the Commissioner of Insurance.

Section 5. MINIMUM STANDARD OF PERFORMANCE.

All insurers shall maintain their affairs so that no unfair claim settlement practices are committed and the State Board of Insurance does hereby declare that the minimum standard of performance for all insurers (as that term is used in Article 21.21-2 of the Insurance Code) is compliance with the provisions of Section 3 of these regulations.

This Order is based upon the necessities and opinion of the Board as to need to protect the public of this State as shown in prior public hearing. This Order may be altered by further Order of the State Board of Insurance

to provide such additional material and to otherwise alter provisions of this Order as the State Board of Insurance deems necessary concerning the matters raised at said hearing

STATE BOARD OF
INSURANCE

/s/ JOE CHRISTIE
Joe Christie, Chairman

/s/ NED PRICE
Ned Price, Member

/s/ DURWOOD MANFORD
Durwood Manford, Member

Recommended and Prepared by:

/s/ DON B. ODUM
Don B. Odum
Commissioner of Insurance

STATE BOARD OF INSURANCE
STATE OF TEXAS

(S E A L)

IT IS HEREBY CERTIFIED That the instrument which is hereunto attached is a true, full and correct copy of Official Order No. 41060 of the State Board of Insurance of the State of Texas, dated June 4, 1982, consisting of three (3) pages; Subject Considered:

> AMENDMENT OF THE PERMANENT AND GENERAL RULES AND REGULATIONS OF THE STATE BOARD OF INSURANCE AS FILED WITH THE TEXAS REGISTER DIVISION, OFFICE OF THE SECRETARY OF STATE, BY AMENDING THE RULES AND REGULATIONS OF THE STATE BOARD OF INSURANCE OF TEXAS ON UNFAIR COMPETITION AND UNFAIR PRACTICES OF INSURERS, AND ON MISREPRESENTATION OF POLICIES, AND INCLUDING REGULATION OF INSURANCE TRADE PRACTICES IN RESPECT OF ADVERTISING AND SOLICITATION (BOARD ORDER 18663) RULES 059.50.-01.001 - .005

now on file in and forming a part of the records of the State Board of Insurance.

IN WITNESS WHEREOF, I hereunto subscribe my name and affix the Seal of the State Board of Insurance, in the City of Austin, State of Texas, this

29th day of April, 1985

JAMES W. NORMAN
Chief Clerk

By: /s/ JAMES W. NORMAN
Custodian of the Record

No. 41060

RECORD OF OFFICIAL ACTION

of the

STATE BOARD OF INSURANCE

AUSTIN, TEXAS

Date: June 4, 1982

Subject Considered: AMENDMENT OF THE PERMANENT AND GENERAL RULES AND REGULATIONS OF THE STATE BOARD OF INSURANCE AS FILED WITH THE TEXAS REGISTER DIVISION, OFFICE OF THE SECRETARY OF STATE, BY AMENDING THE RULES AND REGULATIONS OF THE STATE BOARD OF INSURANCE OF TEXAS ON UNFAIR COMPETITION AND UNFAIR PRACTICES OF INSURERS, AND ON MISREPRESENTATION OF POLICIES, AND INCLUDING REGULATION OF INSURANCE TRADE PRACTICES IN RESPECT OF ADVERTISING AND SOLICITATION (BOARD ORDER 18663) RULES 059.50.01.001 - .005

General remarks and official action taken:

On this day came on for consideration by the State Board of Insurance, amendments to the "Rules and Regulations of the State Board of Insurance of Texas on Unfair Competition and Unfair Practices of Insurers, and on Misrepresentation of Policies, and Including Regulation of Insurance Trade Practices in Respect of Advertising and Solicitation." The amendments contain minor editorial changes, delete surplus and unnecessary language

and correct typographical errors contained in the rules when they were filed as existing rules with the *Texas Register* at or about the time the Administrative Procedure and Texas Register Act went into effect. The amendments are primarily editorial and nonsubstantive and do not change the Board's practices. One correction of a typographical error changes Rule 059.50.01.004(1) to conform to statutory law. Although only rules 059.50.-01.001, .004(1) and .005 are amended, the entire set of rules are reproduced in this Order. It is the opinion of the Board that the amendments should be adopted.

The amendments were published as proposals in the February 19, 1982 edition of the *Texas Register* (7 Tex. Reg. 688). No comments were received. The amendments are enacted under authority of Articles 21.20 and 21.21 of the Texas Insurance Code, and other applicable provisions of the Code which authorize the Board to promulgate rules and regulations to specify and prohibit unfair competition and unfair practices in the business of insurance; and pursuant to the Board's authority to make nonsubstantive editorial clarifications and changes in its rules which are necessary or appropriate for the Board to carry out its statutory duties. It is certified that the amendments as adopted have been reviewed by legal counsel and found to be a valid exercise of the agency's legal authority.

IT IS THEREFORE the Order of the State Board of Insurance that Rules 059.50.01.002, .003 and .004 (2) - (5) be reproduced and Rules 059.50.01.001, .004(1) and .005 be and the same are hereby amended, ordered and prescribed to read as follows:

SECTION 1. The following RULES AND REGULATIONS are ADOPTED, PRESCRIBED AND ORDERED by the State Board of Insurance.

> "Rules and Regulations of the State Board of Insurance of Texas On Unfair Competition and Unfair Practices of Insurers and on Misrepresentation of Policies, and Including Insurance Trade Practices in Respect of Advertising and Solicitation
> 059.50.01.001 - .005."

.001. Deceptive Acts or Practices of Insurers, Agents and Connected Persons. Purpose of Regulation. It is the purpose these Rules and Regulations to further define and state the standards that are necessary to prohibit deceptive acts or deceptive practices by insurers and insurance agents and other persons in their conduct of the business of insurance or in connection therewith, whether done directly or indirectly, and irrespective of whether the person is acting as insurer, principal, agent, employer, or employee, or in other capacity or connection with such insurer.

.002. Interpretations. The meanings given to the provisions, terms and words of this regulation are not to be limited to the common law meaning which may have been given thereto but are to be interpreted to accomplish the purpose of these rules and regulations in accordance with the provisions of Section 13 of Article 21.21 of the Insurance Code.

.003. Unfair Trade Practices Prohibited. (a) Misrepresentation of insurance policies, unfair competition, and unfair practices by insurers, agents and other connected persons are prohibited by Article 21.20 and

Article 21.21 or by other provisions of the Insurance Code of Texas and by the rules and regulations of the State Board of Insurance. No person shall engage in this State in any trade practice that is a misrepresentation of an insurance policy, that is an unfair method of competition, or that is an unfair or deceptive act or practice as defined by the provisions of the Insurance Code of Texas or as defined by these and other Rules and Regulations of the State Board of Insurance authorized by the Code.

(b) Irrespective of the fact that the improper trade practice is not defined in any other section of these Rules and Regulations, no person shall engage in this State in any trade practice which is determined pursuant by law to be an unfair method of competition or an unfair or deceptive act or practice in the business of insurance.

.004. Misrepresentation Defined. Standards for Determining Misrepresentation. The term misrepresentation, or the prohibited conduct, act or practice that constitutes misrepresentation by a person subject to the provisions of this regulation, is defined as any one of the following acts or omissions:

(1) any untrue statement of a material fact; or

(2) any omission to state a material fact necessary to make the statements made (considered in the light of the circumstances under which they are made) not misleading; or

(3) the making of any statement in such manner or order as to mislead a reasonably prudent person to a false conclusion of a material fact; or

(4) any material misstatement of law; or

(5) any failure to disclose any matter required by law to be disclosed, including failure to make disclosure in accordance with the provisions of these and other applicable regulations of the State Board of Insurance.

.005. Enforcement. The Commissioner shall cause to be brought such legal action as is authorized by the Code in the enforcement of these regulations and cause to be enjoined misrepresentations and other unfair trade practices."

SECTION 2. The above Rules and Regulations are ORDERED by the State Board of Insurance; and this Order shall be in full force and effect from and after the date of its signing, and the Rules and Regulations, subject to their provisions, from and after twenty days from the date of filing with the Texas Register Division of the Secretary of State.

This Order remains open for any amendments, corrections, additions or other changes which be made or ordered by the Board.

AND IT IS SO ORDERED.

STATE BOARD OF
INSURANCE

/s/ W. P. DAVES, JR.
W. P. Daves, Jr., Chairman

/s/ DURWOOD MANFORD
Durwood Manford, Member

/s/ LYNDON L. OLSON, JR.
Lyndon L. Olson, Jr., Member

RECOMMENDED AND PREPARED BY:

/s/ A. W. POGUE
A. W. Pogue, Division
Manager, Policy Approval

/s/ JAMES W. NORMAN
James W. Norman
Chief Clerk

Supreme Court, U.S.
FILED
NOV 4 1986
JOSEPH F. SPANIOL, JR.
CLERK

(2)

No. 86-583

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

JIM AUSTIN and AULEMIC, INC.
Petitioners,
vs.
LEXINGTON INSURANCE COMPANY
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF IN OPPOSITION

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**Counsel of Record*

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QUESTIONS PRESENTED

1. Whether the court of appeals correctly applied existing Texas law in this case.

2. Whether there is presented in this case a sufficient question for review by this Court.

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No. 86-583

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

JIM AUSTIN and AULEMIC, INC.
Petitioners,
vs.
LEXINGTON INSURANCE COMPANY
Respondents.

On Writ of Certiorari to the United States
Court of Appeals for the Fifth Circuit

BRIEF IN OPPOSITION

STATEMENT OF THE CASE

Petitioners' statement of the case is erroneous. It includes several versions of fact which were argued for below by Petitioner, but which either were not found below or were reversed by the court of appeals. It also inaccurately states the action of the court of appeals.

The opinion by the court of appeals[1] correctly indicates that no long term charter was in effect between Austin and Servac, and that Servac's refusal further to employ the vessel was unrelated to any action of Lexington.[2] Furthermore, the court of appeals correctly states

[1] 794 F.2d. 941 (5th Cir. 1986); page 5a, Petition Appendix A.
[2] 794 F.2d. at 946; page 15a, Petition Appendix A.

the sequence of actions by Lexington, which did not include a denial of coverage based on a misstatement of maritime law, or a summary closing of the claim file.[3] Lastly, the court of appeals did not refuse to apply Texas law, but simply reached the conclusion that applicable Texas law did not provide a cause of action for treble damages to the insured on the facts of this case.[4]

SUMMARY OF THE ARGUMENT

Contrary to the contentions of Petitioner, the court of appeals reached a principled decision correctly applying amply established Texas authority, their own rules of decision, and the decisions of this Court. Consequently, there is no basis or reason for review by this Court.

REASONS FOR DENYING THE WRIT

I.

The Court of Appeals Correctly Applied Texas Law As Established By Substantial Authority To Conclude That Petitioner Had No Cause Of Action For Treble Damages On The Facts Of This Case.

If the court of appeals made any error in their opinion, it was in citing only the most recent opinions of Texas courts of appeal which hold that Article 21.21 of the Texas Insurance Code, upon which Petitioner relies, does not provide the insured a cause of action for treble damages for unfair claim settlement. The court of appeals cited *Texas Farm Bureau Mutual Insurance Co. v. Vail*[5] and *Chitsey v. National Lloyds Insurance Co.*[6]. They also

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[3] 794 F.2d. at 942; page 5a, Petition Appendix A.

[4] 794 F.2d. at 947-949; pages 18a-20a, Petition Appendix A.

[5] 695 S.W. 2d. 692 (Tex. App.—Dallas 1985, writ requested).

[6] 698 S.W. 2d. 766 (Tex. App.—Austin, 1985, writ granted).

cited two federal district court opinions from Texas, *Lexington Insurance Co. v. Bennett Evans Grain Co.*[7] and *South Texas National Bank of Laredo v. United States Fire Insurance Co.*[8].

All four of the cases relied upon by the court of appeals are based upon the substantial body of decisional law in the Texas courts of appeal reaching back to 1977, shortly after the enactment in 1973 of the Texas Unfair Claim Settlement Practices Act[9]. The earlier cases in the Texas courts of appeal were collected by the U.S. district court for the Northern District of Texas in *McKnight v. Ideal Mutual Insurance Co.*[10]. These earlier cases include: *Hi-Line Electric Co. v. Travelers Insurance Co.*[11]; *Alvarez v. Westchester Fire Insurance Co.*[12]; *Lone Star Life Insurance Co. v. Griffin*[13]; and *Russell v. Hartford Casualty Insurance Co.*[14].

Of the more recent Texas courts of appeal cases, *Vail* relies upon *McKnight* and the authorities cited therein, and upon *Lone Star*[15]. *Chitsey* relies upon *Vail.* A subsequent 1986 Texas court of appeals opinion to the same effect, *Christensen v. Integrity Insurance Co.*[16], relies

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[7] No. G-84-184 (S.D. Tex. Feb. 27, 1986), unreported, copy in Appendix A.

[8] No. L-83-34 (S.D. Tex. Jan. 10, 1985), unreported, copy in Appendix B.

[9] Article 21.21-2, Texas Insurance Code.

[10] 534 F.Supp. 362 (N.D. Tex. 1982).

[11] 587 S.W. 2d. 488 (Tex. Civ. App.—Dallas, 1979), writ ref'd. n.r.e. 593 S.W. 2d. 953 (Tex. 1980).

[12] 562 S.W. 2d. 263 (Tex. Civ. App.—San Antonio) rev'd other grounds, 576 S.W. 2d. 771 (Tex. 1978).

[13] 574 S.W. 2d 574 S.W. 2d. 576 (Tex. Civ. App.—Beaumont 1978, writ ref'd n.r.e.).

[14] 548 S.W. 2d. 737 (Tex. Civ. App.—Austin, 1977, writ ref'd n.r.e.).

[15] Supra, notes 5, 10 and 13.

[16] 709 S.W. 2d. 724 (Tex. App.—Houston [14th District] 1986), rev'd. on other grounds ___ S.W. 2d. ___, 30 Tex. Supp. Ct. Jour. 37 (1986).

upon *Lone Star*[17]. In the federal courts, *Bennett Evans* relies on *McKnight* and the cases collected therein, and upon *Vail* and *Chitsey.*[18] *National Bank of Laredo* relies upon *Lone Star* and *Hi-Line Electric.*[19]

A detailed discussion of the holdings in each of these cases would be lengthy. Such a discussion would also be largely irrelevant to the question before this Court because the rationale of each case and the precise holdings vary, depending both on the facts presented and the variations in the possible application of Texas common law, Texas statutes, and administrative regulation which were suggested by the ingenuity of counsel. The most comprehensive review of the possible causes of action under Texas common law, the Texas Insurance Code, the Texas Deceptive Trade Practices Act, their interlocking provisions, and the orders of the Texas Insurance Board, in the context of a claim against a property insurer, is found in *Bennett Evans Grain*[20]. A review of that case, and the others cited above, leads inevitably to the conclusion that there is no statute or combination of statutes and Texas common law under which a property insurer is liable to the assured for treble damages for improper handling of a claim, much less for failure to pay a disputed claim. A remedy for unfair claims handling *practices* is reserved to the Texas Insurance Board. This is particularly true where, as in the instant case, no claim is made under Texas common law or the Texas Deceptive Trade Practices Act, and reliance is placed on Article 21.21, Texas Insurance Code, and the board orders.

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[17] Supra note 13.

[18] Supra notes 5, 6, 7, 10.

[19] Supra notes 8, 11, 13.

[20] Appendix A, pp. A-5 to A-10.

Texas authority to the effect just discussed is consistent. It is quite incorrect to assert, as does Petitioner, that *Royal Globe Insurance Company v. Bar Consultants, Inc.*[21], is applicable to this case, or involves the identical violation as in the instant action.[22] In noting that the Texas decisions were consistent on the inapplicability of Article 21.21 to unfair claim settlement cases[23], and omitting reference to *Royal Globe,* the court of appeals paralleled the reasoning of the district court in *McKnight*[24], which specifically pointed out the inapplicability of *Royal Globe* to a claim for improper claims handling, accurately describing and distinguishing *Royal Globe* as a misrepresentation case.[25] The district court in *National Bank of Laredo* did the same.[26] *Royal Globe* involved misrepresentation by an agent to an assured of the coverage of a policy both before and after a loss occurred. It is likewise entirely incorrect to argue, as does Petitioner, that in *Mayo v. John Hancock*[27], the Texas supreme court held that Art. 21.21(16) allows a private cause of action for treble damages. *Mayo* involved a summary judgment on the issue of whether recovery of actual damages under Art. 3.62 of the Texas Insurance Code barred the recovery of damages under Art. 21.21(16) or the Texas Deceptive Trade Practices Act. The Texas supreme court held that the Texas court of appeals had misinterpreted § 17.43 of the Texas Deceptive Trade Practices Act, and disclaimed any ruling on the question of treble damages under the Texas Insurance Code and the Deceptive Trade Practices Act.[28]

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21 577 S.W. 2d. 688 (Tex. 1979).

22 Petition p. 8, Note 10.

23 794 F.2d., 949, Note 8; page 20a, Petition Appendix A.

24 Supra, note 10.

25 534 Fed. Supp. at 366.

26 Appendix B, p. B-4.

27 711 S.W. 2d. 5 (Tex. 1986).

28 711 S.W. 2d. at 7.

Since the two decisions from the Texas supreme court cannot be characterized as they are by Petitioner, it follows that the court of appeals most certainly did not, as argued by Petitioner, render a decision contrary to decisions of the Texas supreme court.[29] The statement by Petitioner that the holding of the district court was based on decisions from the Texas supreme court "which have uniformly awarded treble damages against insurers engaging in unfair claim settlement practices"[30] is likewise erroneous. The district court cited only *Royal Globe,* an inapplicable case already discussed.

At various stages of review by the court of appeals, Petitioner argued other cases in the Texas courts of appeal in support of his position: *Allstate Insurance Co. v. Kelley*[31]; *St. Paul Insurance Company v. McPeak*[32]; *Aetna v. Marshall*[33]; and *Arnold v. National County Mutual Fire Insurance Co.*[34]. *McPeak* is a workman's compensation case in which, as pointed out by the court of appeals[35], the assured brought suit after the insurer terminated his workmans compensation benefits. The Court specifically disclaimed a ruling on the Article 21.21 issue[36]. *Kelley* is a case involving negligent mishandling by a liability insurer of automobile litigation brought by a third party against

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[29] Petition, p. 5.

[30] ibid.

[31] 680 S.W. 2d. 595 (Tex. App.-Tyler, writ ref'd. n.r.e.).

[32] 641 S.W. 2d. 284 (Tex. App.-Houston [14th District] 1982, writ ref'd. n.r.e.).

[33] 699 S.W. 2d. 896 (Tex. App.-Houston [1st Dist.] 1985, writ granted).

[34] (Tex. App.-Houston [1st Dist.] August 22, 1985, writ granted) not reported, copy in Appendix C.

[35] 794 F.2d. at 949, note 8; page 20a, note 8, Petition Appendix A.

[36] 641 S.W. 2d. 288.

an assured. Like *McPeak*, it was correctly distinguished by the court of appeals because it did not involve a property insurer[37] and because it arose from a problem other than claim handling. *Marshall* is another workman's compensation case, involving the enforcement of a judgment requiring an insurer to pay future medical expenses. It is not mentioned in the court of appeals opinion, presumably because it shares the same distinctions as *McPeak* and does not involve claim handling. *Arnold* involves a summary judgment on a statute of limitations issue and an issue of Texas common law regarding an implied duty of good faith and fair dealing not presented in the instant case. The Texas Supreme Court will review only those issues.[38]

In short, as the court of appeals points out,[39] the decisions of the Texas courts of appeal, rather than being split on the question of the applicability of treble damages to claim handling under Article 21.21 of the Texas Insurance Code, are consistent. As is apparent from a reading of its opinion, the court of appeals reviewed the applicable Texas case law as submitted by the parties in reaching their decision.

The assertion by Petitioner that the court of appeals created an exception for a marine property insurer, and declined to apply the Texas statute on the basis that the policy involved was one of marine insurance[40] are quite unfounded. Nowhere in the opinion of the court of appeals is any such reasoning to be found. The court of appeals correctly begins their analysis with *Wilburn Boat v. Fireman's Fund,*[41] and goes on to analyze Texas and

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[37] 794 F.2d. at 949, note 8; page 20a, note 8, Petition Appendix A.

[38] 29 Tex. Sup. Ct. Jour. 78.

[39] 794 F.2d. at 949, n. 8; page 20a, note 8, Petition Appendix A.

[40] Page 6 of Petition.

[41] 348 U.S. 310 (1955); 794 F.2d. at 948; page 18a, Petition Appendix A.

Florida state law. Their analysis repeatedly refers to the question of "whether Article 21.21 applied to a property insurer who failed to fairly handle a claim made by his insured"[42]. There is no distinction whatever made between a marine property insurer and any other property insurer.

Given the state of the law of Texas as set out above and as relied upon by the court of appeals, the court of appeals had ample precedent upon which to base its decision as to the law of Texas. In reaching its conclusion, the court of appeals relied on its own rule of decision, which holds that a decision of a Texas court of civil appeals is controlling on questions of Texas law in the federal court of appeals, absent a strong indication the Texas supreme court would decide the issue differently.[43] Given the substantial authority from Texas courts of appeal and the absence of any contrary authority, there could have been no justification for the court of appeals to certify the question to the Texas supreme court, as Petitioner urges should have been done.

Were it necessary to speculate on the possible action of the Texas supreme court, as the court of appeals would have been obliged to do had there been no authority from the Texas courts of appeal available to them, the Texas writ history of the Texas cases cited above would be instructive. The Texas supreme court can be seen to have undertaken to review a series of cases, recently decided,

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[42] e.g., 794 F.2d. at 948; page 19a, Petition Appendix A.

[43] *Birmingham Fire Insurance Co. v. Weingardner,* 714 Fed. 2d. 548 (5th Cir. 1983); *Mott v. Mitsubishi International,* 636 Fed. 2d. 1073 (5th Cir. 1981) and cases cited therein; *Continental Grain Co. v. Martin,* 536 Fed. 2d. 592 (5th Cir. 1976) cert. denied 429 U.S. 1024 (1976). Judge Brown's comments on the merits of certification, alluded to on page 9 of the Petition, are directed to situations in which a "guess" on an unclear point is involved, and pre-date the two more recent of these cases.

which involve various kinds of insurers, including property, and the question of treble damages under the complex interface created by Texas common law, various provisions of the Texas Insurance Code, the Texas Deceptive Trade Practices Act, and various administrative regulations issued thereunder or incorporated therein. The wide variety of factual situations and the wide variety of legal situations created by the variations in pleading and proof reviewed by the Texas courts of appeal have tended to create a gray area which lies between the clear misrepresentation of policy coverage present in *Royal Globe*[44] and the straightforward assignment of the cause of action for unfair claims handling practices to the State Board of Insurance under the Texas Unfair Claims Settlement Act.[45] The cases taken up consistently involve claims under the Texas Deceptive Trade Practices Act as well as the Texas common law question of the existence of an implied duty of good faith and fair dealing, neither of which are involved in the instant case. *Chitsey*, of which Petitioner makes much, as well as ruling on Article 21.21, has the latter issue. Given the existing condition of Texas authority regarding Article 21.21 discussed earlier, it is entirely erroneous to charge the court of appeals with having reached out to decide prematurely a new question before the Texas Supreme Court, as does Petitioner. It would appear most unlikely that the Texas supreme court would go so far as to upset ten years of jurisprudence in the Texas courts of appeal and allow treble damages for the simple non-payment of a disputed claim. It is far more likely that they would undertake a line-drawing exercise to set a boundary between the two extremes and eliminate the possibility of decisions such as that of the federal district court in the instant case, which was correctly reversed by the federal court of appeals.

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[44] Supra, note 19.

[45] Supra, note 9.

II.

The Instant Case Presents No Constitutional Issue, Issue Of Federalism, Of Uniformity Of Maritime Law, Or Any Other Issue Meeting The Standard For Review By This Court.

As pointed out in I above, and as plainly stated in the opinion, the court of appeals duly followed the guidance of *Wilburn Boat v. Fireman's Fund,*[46] as interpreted by *Kossick v. United Fruit Co.,*[47] in applying state law to a policy of marine insurance in the absence of a controlling federal rule on the subject.[48] In addressing the applicability of the Texas statute, the court of appeals makes no mention of the marine character of the policy at issue in concluding that the statute does not confer a cause of action. Thus, there is no issue presented here of failure to follow the dictates of this Court regarding the applicablity of state law to policies of marine insurance, or the oft-repeated admonitions of this Court on the subject of the desirability of uniformity in the maritime law and the law of marine insurance.

Because there is no such case, Petitioner cites no case to indicate that any other circuit court of appeals has decided differently a case dealing with this aspect of Texas law.

The decisional rule of the Fifth Circuit regarding matters of Texas law, as developed by circuit judges many of whom were Texas lawyers, provides a rational basis on which the court of appeals may act to resolve a case before it.[49] Following the guidance of that rule to resolve matters of Texas law to which the Texas courts of appeals have spoken, but the Texas supreme court has not, and where

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[46] 348 U.S. 310 (1955).
[47] 365 U.S. 731 (1961).
[48] 794 F.2d. at 948; page 18a, Petition Appendix A.
[49] Supra, note 43.

there is no indication of the position of the Texas supreme court, can hardly be characterized as reaching out to decide prematurely a question of state law, as Petitioner argues. This case in no way involves a decision by the court of appeals of a question on which substantial and uniform Texas authority is not available, and therefore in no way involves the situation presented by *Railroad Commission of Texas v. Pullman*[50], as Petitioner argues.

Despite the strained arguments which Petitioner puts forward in an effort to create one, it is quite apparent that there are no issues presented in the case as decided by the court of appeals which meet the standards of Rule 17 of the rules of this Court or any of the other criteria of national importance for review by this Court.

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[50] 312 U.S. 496 (1941).

CONCLUSION

The requested writ of certiorari to the court of appeals for the Fifth Circuit should be denied for the following reasons:

1. The United States Court of Appeals for the Fifth Circuit reached a principled and correct decision based on ample precedent in the jurisprudence of the State of Texas. In particular, there is no indication that there will be any change in the law of Texas on the point on which they rested their decision.

2. Under the circumstances of the case, there can be no question presented meeting the standards of national importance for review by this Court.

Respectfully submitted,

By_____

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CERTIFICATE OF SERVICE

I hereby certify that I have served three copies of the above and foregoing brief by mailing them by certified mail, return receipt requested, to David S. Prince, Esq., 5400 Memorial Drive, Suite 103, Houston, Texas 77007.

_____

E. J. Silva

APPENDIX A

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
GALVESTON DIVISION

C. A. G-84-184

LEXINGTON INSURANCE COMPANY

vs.

BENNETT EVANS GRAIN COMPANY, ET AL

MEMORANDUM AND ORDER

This controversy began as a suit for declaratory judgment on an insurance contract. Today this cause also involves claims under the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961-1968: article 21.21 of the Texas Insurance Code ("TIC"); and section 17.50 of the Texas Deceptive Trade Practices Act ("DTPA").

I.

Lexington Insurance Company ("Lexington") insured the property of Bennett Evans Grain Company ("Bennett"). Bennett stored grain for the Commodity Credit Corporation ("CCC") a division of the United States Department of Agriculture.[1] In August, 1983, Hurricane Alicia damaged Bennett's facilities. Bennett duly reported the loss to Lexington. Bennett claims that Alicia destroyed property including Building No. 2, its main storage building, and the grain stored therein. Lexington and Bennett settled the claims for damage to other Bennett property. Bennett claims that Lexington, through ABJ Adjusters, Inc. ("ABJ"), agreed that approximately $450,000.00 would settle the claim for Building No. 2 and the grain. Lexington allegedly rejected this amount and discharged ABJ. Lexington asserts that it questioned the extent of the claimed damage and whether part of the damage existed prior to Alicia.

[1] The CCC is not a party to this litigation.

Lexington retained GAB Business Services, Inc. ("GAB"). GAB's agent, Joseph Bonanno negotiated unsuccessfully with Bennett regarding Building No. 2 and the grain. Bennett claims that Bonanno agreed that the grain could be partially salvaged at a cost of $49,000.00 but that Lexington also wrongfully rejected this settlement. At Bonnano's request, the parties met on April 10, 1984. Jim Bennett, apparently the sole owner of Bennett, stated in deposition that Bonnano made him the following offer at the meeting:

> I'm not entertaining a claim on the [grain] at all. I will put a new face on your building and give you $100,000.00 to settle the entire claim. . . . You know, it's going to be awhile before you get a claim from CCC. Take the money and use it as you see fit.

Jim Bennett refused, negotiations broke down, and Bonnano allegedly sent a letter to CCC indicating that there was little damage to the grain and that settlement was unlikely.[2]

Lexington then filed this suit for declaratory judgment and to enjoin Bennett to allow inspection of the damaged premises. Bennett counterclaimed under the insurance contract, the DTPA, the TIC, and RICO, and impleaded GAB and Bonanno under RICO.

GAB and Bonnano move for summary judgment. Lexington moves for summary judgment on all claims other than the action on the insurance contract. Bennett moves to compel discovery; to strike Lexington's pleadings and for default or, in the alternative to require Lexington to deposit funds in the registry of the court; and for partial

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[2] In its third amended counter-claim and third-party claim, Bennett attempted to add a claim for tortious interference with a business relationship based on the letter to the CCC. The Court denied this motion for leave to amend. Thus, the Court now disregards any claims of damage based on tortious interference.

summary judgment. Pursuant to the standard for summary judgment set forth in *Harrison v. Byrd,* 765 F.2d 501, 504 (5th Cir. 1985), the Court grants the summary judgment motions of Lexington, GAB and Bonnano, and denies the summary judgment motion of Bennett. The Court denies Bennett's motions to compel and to strike. The Court first turns to Bennett's RICO claim.

II.

The gravaman of plaintiff's RICO action is the requirement of "at least two acts of racketeering activity" to demonstrate the required "pattern of racketeering activity." 18 U.S.C. § 1961(6). Bennett alleges three indictable predicate acts as defined in 28 U.S.C. § 1961(1)(B): 1) a bribe under 18 U.S.C. § 201, 2) mail fraud under 18 U.S.C. § 1341, and 3) wire fraud under 18 U.S.C. § 1343. Factually, these predicate acts stem from Bonnano's offer of $100,000.00 which plaintiff characterizes as an attempted bribe. The Court, of course, is not bound by Mr. Bennett's characterization of the events. Instead, the Court looks at the law and the evidence submitted by the parties.

Bribery under 18 U.S.C. § 201 requires an offer of something of value to a government official with the intent to influence some official act or have the official otherwise betray his public trust. *E.g., Parks v. United States,* 355 F.2d 167 (5th Cir. 1965) (per curiam). In deposition Jim Bennett stated that the offer of $100,000.00 and to put a new face on the building was a ridiculously low offer of settlement. Bennett alleges that Bonnano made the offer "behind the back" of the CCC, the owner of the grain. Yet Jim Bennett stated that even if he accepted the offer, he would still eventually have to pay the government for the damaged grain. Bennett's building with a new face—presumably, according to the deposition testimony,

replacing the tin facing blown off by Alicia—would still be damaged if Alicia had damaged more than the facing. Bennett has not attempted to show that the building belonged to another party. Bennett was the only beneficiary of the insurance policy.[3] Thus, Jim Bennett's statements thus raise an interesting question: why and how would an insurer bribe the insured to act against his own financial interests in settling his claim? The answer, of course, is that he could not. This scenario does not reveal an indictable act of bribery.

Assuming, however, that the offer was an attempted bribe, it was only one act. Jim Bennett stated in deposition that only at the meeting did Bonnano offer him a "bribe." If Bonnano had also made Bennett the offer over the telephone, *R.A.G.S. v. Couture, Inc. v. Hyatt,* 774 F.2d 1350, 1354-55 (5th Cir. 1985), might compel this Court to find two predicate acts. In *R.A.G.S.,* the plaintiff alleged that defendant or its lawyer twice mailed plaintiff the same fraudulent invoices. The trial court dismissed plaintiff's RICO action on the grounds plaintiff had not alleged or shown a pattern of racketeering activity because there was only one predicate act of mail fraud. The Court of Appeals reversed, holding that plaintiff factually alleged two indictable acts of mail fraud. *Id.* Here, a telephone call arranging a meeting or a letter discussing settlement is not a separately indictable act of bribery sufficient to establish a pattern of racketeering activity under *R.A.G.S.*

Bennett also alleges that Lexington, GAB, and Bonnano delayed settlement to force Bennett to settle its claim for less than its fair value as a result of financial pressures on Bennett. Bennett alleges that Lexington, GAB, and

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[3] Alvin State Bank intervened in this suit. This Bank claims that Bennett assigned all of its rights and interest in the insurance policy to the Bank on November 20, 1984. This was after the events giving rise to the alleged RICO claim.

Bonnano used the mails and telephone to further this "conspiracy" and to arrange the meeting where Bonnano attempted to bribe Mr. Bennett. Bennett contends that these are indictable acts of mail fraud, 18 U.S.C. § 1341, and wire fraud, 18 U.S.C. § 1343. A scheme to defraud is an essential element of both offenses. *E.g., United States v. Schaffer,* 559 F.2d 678 (5th Cir. 1979) (per curiam) (mail fraud); *United States v. Foley,* 683 F.2d 273 (8th Cir. 1982) (wire fraud). Fraud consists of a false representation or material nondisclosure "reasonably calculated to deceive persons of ordinary prudence and comprehension." *Schaffer,* 559 F.2d at 679. Although Bennett's allegations suggest deplorable conduct in settling an insurance claim on the part of Lexington and its agents, the allegations do not show a scheme to defraud.

In conclusion, Bennett's RICO claims must be dismissed because Bennett fails to establish at least two predicate acts of racketeering activity pursuant to 18 U.S.C. § 1961.

III. Bennett's Texas Statutory Claim

Bennett sues pursuant to the Unfair Competition and Unfair Practices Act ("UCUPA"), Tex.Rev.Civ.Stat.Ann. art. 21.21, § 16 (Vernon 1981), and the DTPA, Tex.Rev.Civ.Stat.Ann. § 17.50 (Vernon Supp. 1986) for treble damages and attorneys' fees for unfair settlement practices and unconscionable conduct in the settlement of an insurance claim.

The issue requires the Court to interpret three interlocking, concurrently enacted consumer protection statutes. In 1973, the 63rd Texas Legislature enacted the DTPA, section 16 of article 21.21, and the Unfair Claim Settlement Practices Act ("UCSPA"), Tex.Rev.Civ.Stat.Ann. art. 21.21-2 (Vernon 1981). *See*

generally Comment, *An Insurer's Failure to Settle: Standing Under the Stowers Doctrine, Texas Deceptive Trade Practice Act, and Article 21.21 of the Insurance Code,* 34 Baylor L. Rev. 441 (1982) [hereinafter cited is *Comment*]. The Court therefore adheres to the requirement that it construe together concurrently enacted and in pari materia legislation. *Duval Corp. v. Sadler,* 407 S.W.2d 493 (Tex. 1966): *State v. Dyer,* 200 S.W.2d 813 (Tex. 1947).

The DTPA, article 21.21, and article 21.21-2, authorize state agencies to investigate and sanction statutory violations. Section 17.50 of the DTPA[4] and section 16 of

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[4] Tex.Rev.Civ.Stat.Ann. § 17.50 (Vernon Supp. 1986) provides in relevant part:

> (a) A consumer may maintain an action where any of the following constitute a producing cause of actual damages:
>
> (1) the use or employment by any person of a false, misleading, or deceptive act or practice that is specifically enumerated in a subdivision of Subsection (b) of Section 17.46 of this subchapter;
>
> (2) breach of an express or implied warranty;
>
> (3) any unconscionable action or course of action by any person; or
>
> (4) the use or employment by any person of an act or practice in violation of Article 21.21, Texas Insurance Code, as amended, or rules or regulations issued by the State Board of Insurance under Article 21.21, Texas Insurance Code, as amended.
>
> (b) In a suit filed under this section, each consumer who prevails may obtain:
>
> (1) the amount of actual damages found by the trier of fact. In addition the court shall award two times that portion of the actual damages that does not exceed $1,000.00. If the trier of fact finds that the conduct of the defendant was committed knowingly, the trier of fact may award not more than three times the amount of actual damages in excess of $1,000.00. . . .

article 21.21[5] explicitly provide consumers with a private cause of action and the possibility of treble damages and attorneys' fees. Article 21.21-2, on the other hand, does not create a private cause of action; it only authorizes the Texas Board of Insurance Commissioners ("Board") to investigate and sanction unfair claims settlement practices. *See McKnight v. Ideal Mutual Insurance Co.*, 534 F.Supp. 362, 364 (N.D. Tex. 1982) (collecting Texas cases). Beyond the simple lack of language creating a private cause of action, this conclusion makes sense. Article 21.21-2 prohibits unfair claim settlement *practices*. Section 2 of 21.21-2 explicitly states that the unfair claim settlement acts must be committed with sufficient frequency to actually be a practice. Tex.Rev.Civ.Stat.Ann. art. 21.21-2, § 2 (Vernon 1981). Thus, a private cause of action for one unfair settlement would be inconsistent with section 2.

Bennett does not proceed directly under article 21.21-2. Rather, Bennett asks the Court to find a private cause of action the DTPA and the UCUPA. Because the Texas Supreme Court has not addressed this question, the Court must make an *Erie*-guess and rule as it believes that the

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[5] Tex.Rev.Civ.Stat.Ann.art.21.21, § 16 (Vernon 1981) provides in revelant part:

> (a) Any person who has been injured by another's engaging in any of the practices declared in Section 4 of this Article or in rules or regulations lawfully adopted by the Board under this Article to be unfair methods of competition and unfair and deceptive acts or practices in the business of insurance or in any practice defined by Section 17.46 of the Business & Commerce Code, as amended, as an unlawful deceptive trade practice may maintain an action against the company or companies engaging in such acts or practices.
>
> (b) In a suit filed under this section, any plaintiff who prevails may obtain:
>
> (1) three times the amount of actual damages plus court costs and attorneys' fees reasonable in relation to the amount of work expended . . . .

Texas Supreme Court would rule. *E.g., Green v. Amerada-Hess Corp.*, 612 F.2d 212, 214 (5th Cir.), *cert. denied*, 449 U.S. 952 (1980). *See generally* 19 C. Wright, A. Miller, & E. Cooper, Federal Practice and Procedure § 4507, at 86-103 (1982).

The Court first looks to the structure of the acts. At least one Texas court has held, and this Court agrees, that the Texas Legislature intended to "seal off" unfair claim settlements from the expansive damage remedies of the DTPA and the TIC. *See Texas Farm Bureau Mutual Insurance Co. v. Vail*, 695 S.W.2d 692, 694 (Tex.Civ.App.—Dallas, 1985, writ requested) (quoting *Comment, supra*, at 455). By enacting 21.21-2, the 63rd Legislature showed that it clearly understood the nature of an unfair claim settlement. The 63rd Texas Legislature also clearly understood how to grant a private cause of action: it did so in section 16 of UCUPA and § 17.50 of the DTPA. By cross-referencing the DTPA and UCUPA, the 63rd Texas Legislature showed that it knew how to expressly import a private cause of action into one statute from another. Yet the Legislature did not create a private cause of action for unfair claim settlements in 21.21-2. Nor did the 63rd Texas Legislature explicitly import 21.21-2 into either the DTPA or the UCUPA.

The Court finally notes that if the DTPA or the UCUPA by their own terms prohibit unfair claim settlements, 21.21-2 is superfluous. The DTPA and the UCUPA authorize state agency action. If they prohibit unfair claim settlements, 21.21-2 authorizes nothing new.

The Court now addresses Bennett's specific arguments. Bennett contends that violations of 21.21-2 are actionable under section 16 of 21.21. The Legislature, however, expressly limited private actions under section 16 to violations of 1) section 4 of article 21.21, 2) the rules and regulation adopted by the Board under article 21.21,

and 3) DTPA section 17.46. The Legislature did not incorporate 21.21-2 into section 4 of article 21.21 and no language in section 4 could be construed to give Bennett a cause of action for a violation of article 21.21-2. *Chitsey v. International Lloyd's Insurance Co.*, 698 S.W.2d 766, 777 (Tex.Civ.App.—Austin 1985, writ requested).

Bennett next argues that it has a cause of action under the second prong of section 16, the Board adopted rules and regulations. The Board promulgated Rules 059.50.01.001-.005, which contain broad language prohibiting "an unfair or deceptive act or practice as defined by the provisions of the Insurance Code of Texas or as defined by these and other Rules and Regulations of the State Board of Insurance authorized by the Code." Bennett argues that this language in effect incorporates an action under article 21.21-2 into section 16. The Court disagrees with this tortious logic. *Cf. Chitsey,* 698 S.W.2d at 770. The rule as interpreted by Bennett would not be authorized by the Code. Unfair claim settlement practices are governed by article 21.21-2 and article 21.21-2 only authorizes Board sanctions, not private actions. Rules 059.50.001-.005 were promulgated under articles 21.20 and 21.21 which do not address unfair claim settlement practices.

Bennett furthermore argues that Rules 059.50.01.001-.005 incorporate Tex.Rev.Civ.Stat.Ann. art. 1.14-2, § 8(b) (Vernon 1981) into section 16. Section 8(b) prohibits an insurance agent from placing insurance with surplus line insurers that are not authorized by the Board to do business in Texas unless, inter alia, the insurer is "of good repute and provide[s] reasonably prompt service to its policyholders in the payment of just losses and claims." Under article 1.14-2, an agent may be penalized for violating article 1.14-2 and an insured may sue for breach of contract. The Court, however, will not contort section 8(a) into an action under section 16 for attorneys fees and

trebel [SIC] damages for an insurer's unfair claim settlement. Neither the rules Bennett relies on nor article 1.14-2 explicitly address an unfair claim settlement.

Bennett then turns to the third prong of section 16 of article 21.21—"any practice defined by section 17.46 of the [DTPA] as an unlawful deceptive trade practice"—and argues that Lexington violated DTPA section 17.46(a). Section 17.46(a) provides: "False, misleading, or deceptive acts or practices in the conduct of any trade or commerce are hereby declared unlawful." Section 17.46(b) lists specific false, misleading, or deceptive acts. Bennett does not allege or show a violation of subsection (b).

The Court begins by noting that when a consumer sues under the DTPA for a false, misleading, or deceptive act or practice, the consumer cannot sue under subsection (a). *See* Tex.Rev.Civ.Stat.Ann. 17.50(a) (Vernon Supp. 1986). Bennett essentially argues that although there is no private cause of action under the DTPA for violations of 17.46(a), the Legislature created one under the TIC in section 16 of article 21.21. The wording of section 16, however, belies this conclusion. It is tantological [SIC] to say that a "[f]alse, misleading, or deceptive act" defines an "unlawful deceptive trade practice." Based on this reasoning, in *Mobile County Mutual Insurance Co. v. Jewell,* 555 S.W.2d 903, 910-11 (Tex.Civ.App.—El Paso 1977, writ ref'd n.r.e.), the court held that the legislature intended that only violations of section 17.46(b) are incorporated into section 16 of article 21.21. *Accord General Accident, Fire and Life Assurance Corp. v. Legate,* 578 S.W.2d 509, 507 (Tex.Civ.App.-Texarkana 1974, no writ). *But see Allstate Insurance Co. v. Kelly,* 680 S.W.2d 595, 605 (Tex.Civ.App.—Tyler 1984, no writ) (citing dicta in *Royal Globe Insurance Co. v. Bar Consultants,* 577 S.W.2d 688 (Tex. 1979)).

Even if the legislature intended to incorporate subsection (a) into section 16, Bennett's claim must be dismissed. A plaintiff under article 21.21, § 16 must allege and show that he was injured as a result of an enumerated violation. Tex.Rev.Civ.Stat.Ann. art. 21.21, § 16(a) (Vernon 1981). Denial of insurance coverage is not a deceptive trade act or practice when the denial does not terminate or lessen the insurer's obligations or extinguish the insured'[s] rights under the insurance contract. *Reed,* 626 S.W.2d at 905; *Legate* 578 S.W.2d at 507; *Lone Star Life Insurance Co. v. Griffin,* 574 S.W.2d 576, 580 (Tex.Civ.App.—Beaumont 1978, writ ref'd n.r.e.). Bennett has not alleged or shown that any act of Lexington has extinguished any of Bennett's rights under the insurance contract.

In *Royal Globe,* 577 S.W.2d 688, 695 (Tex. 1979), the Texas Supreme Court held that in a DTPA suit against an insurer for post-loss representations, the plaintiff must show that he relied on a false, misleading, or deceptive representation and that he was damaged as a result. *Crossland v. Canteen Corp.,* 711 F.2d 714, 726 (5th Cir. 1983); *Jay Freemand Co. v. Glen Falls Insurance Co.,* 486 F.Supp. 140, 142 (N.D. Tex. 1980); *Molinar v. Plains Insurance Co.,* 660 S.W.2d 845, 850 (Tex.Civ.App.—Amarillo 1983, no writ). Plaintiff's alleged damages stem from the loss and Lexington's subsequent denial of the claim, not any representation that Lexington would pay $400,000.00.

In suits directly under the DTPA, section 17.50 provides that the deceptive act must be a "producing cause of actual damage." Furthermore, the plaintiff must be a consumer, one "who seeks or acquires by purchase or lease, any goods or services . . ." Tex.Rev.Civ.Stat.Ann. § 17.45(4) (Vernon Supp. 1986). An insurer's post-loss representations or denial of coverage is not in connection with a purchase or sale; therefore, Bennett is not a

consumer. *Rosell v. Farmers Texas County Mutual Insurance Co.,* 642 S.W.2d 278, 279 (Tex.Civ.App.—Texarkana 1982, no writ); *American Insurance Co. v. Reed,* 626 S.W.2d 898, 902 (Tex.Civ.App.—Eastland 1981, no writ); *Hartford Insurance Co. v. Carroll,* 575 S.W.2d 578, 580 (Tex.Civ.App.—Beaumont 1978, no writ). *But see Ranger County Mutual Insurance Co. v. Ginn,* 608 S.W.2d 730, 731-32 (Tex.Civ.App.—Tyler 1980, writ dismissed).

In conclusion, Bennett's claim under the TIC and the DTPA must be dismissed.

IV. Bennett's Common Law Bad Faith Claim

Bennett asserts a common law cause of action in tort for bad faith. Bennett contends that Lexington breached its implied duty to settle Bennett's claim fairly and in good faith. In *English v. Fischer,* 660 S.W.2d 521, 522 (Tex. 1983), the Texas Supreme Court held that there is no general duty of good faith implied in a contract. In a concurring opinion, Justice Spears noted that the Court was not overruling its recognition of an implied duty of good faith that arises from some special realtionship of the parties. *Id.* at 524. Justice Spears specifically noted *Stowers Furniture Co. v. American Indemnity Co.,* 15 S.W.2d 544 (Tex. Comm'n. App. 1929, opinion adopted), which recognized an insurer's obligation of good faith in settling a suit against the insured when the insurer is defending the action. *See also Aetna Casualty & Surety Co. v. Marshall,* 699 S.W.2d 876 (Tex.Civ.App.—Houston [1st Dist.] 1985, writ requested) (recognizing obligation of good faith of insurer under agreed judgment between insured and insurer).

Bennett's action, however, does not implicate the *Stowers* situation where the insured has a quasi-fiduciary responsibility to the insured. Rather, an insured's claim

under the policy places the parties in direct conflict. This Court holds that under *English,* Lexington has no implied duty to deal fairly and in good faith in adjusting Bennett's insurance claim. *Thompson v. M & B Construction Corp.,* 585 F.Supp. 561 (N.D. Tex. 1984). *See also Cook Consultants, Inc. v. Stewart Title Guaranty Co.,* 677 S.W.2d 718, 720-21 (Tex.Civ.App.—Dallas, 1984, no writ); *Texas Farm Bureau Mutual Insurance Co. v. Vail,* 695 S.W.2d 692, 694 (Tex.Civ.App.—Dallas 1985, writ requested).

V. Bennett's Discovery Motion

Bennett moves to compel discovery of Lexington's files relating to Bennett's claim ("claim file"). Tex.R.Civ.P. 186a prohibits discovery of the claim file. *Maryland American General Insurance Co. v. Blackman,* 639 S.W.2d 455, 457-58 (Tex. 1982). Pursuant to Fed.R.Evid. 501, the Court, therefore, must deny Bennett's motion.

VI. Bennett's Motion to Strike

Bennett moves pursuant to Tex.Rev.Civ.Stat.Ann. art. 1.14-1, § 6(a)1 (Vernon 1981) (unauthorized insurers) to strike and for default, or to require Lexington to deposit into the registry of the Court funds sufficient to secure the payment of a final judgment. The Court, however, finds that Lexington has sufficient assets from which to satisfy an adverse judgment. Therefore, the Court denies plaintiff's motion. Article 1.14-1 § 16(a)1.

VII. Bennett's Partial Summary Judgment Motion

Bennett moves for partial summary judgment for $99,235.00 and attorneys fees. Bennett moves for this amount based on a demand by the CCC made on Bennett for damaged rice that Bennett shipped to it. The Court finds, however, that there are fact issues material to Bennett's claims. The parties have tendered conflicting affidavits on the extent and cause of the damage to the grain. Therefore, the Court must deny Bennett's motion for partial summary judgment.

VIII.

In summary, it is ORDERED, ADJUDGED and DECREED as follows:

1. the motion for summary judgment of GAB and Joe Bonnano is GRANTED;

2. the motion for partial summary judgment of Lexington is GRANTED;

3. Bennett's motion to compel discovery is DENIED;

4. Bennett's motion to strike is DENIED; and

5. Bennett's motion for partial summary judgment is DENIED.

DONE at Galveston, Texas, this the 27th day of February, 1986.

/s/ Hugh Gibson

United States District Judge

APPENDIX B

SOUTH TEXAS NATIONAL BANK OF LAREDO,
Plaintiff,

VS.

UNITED STATES FIRE INSURANCE COMPANY,
Defendant.

CIVIL ACTION NO. L-83-34

UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
LAREDO DIVISION

SLIP OPINION

January 10, 1985

COUNSEL:

Donato D. Ramos, P.O. Box 1262, Laredo, Texas 78041, for Plaintiff

John W. Davidson, Terry Topham, Two Saga Center, 613 NW Loop 410, Suite 1000, San Antonio, Texas 78216, for Defendant

OPINION BY: KAZEN

South Texas National Bank (South Texas) has sued its insurer United States Fire Insurance Company (the company). South Texas seeks to recover under a Banker's Blanket Bond and Excess Fidelity policy (the policy). South Texas asserts that the policy covers its losses caused by the alleged dishonesty and fraudulent acts of its former President, Bristow, and Vice-President, Rios, in connection with loans to Francisco Lerma and his businesses. South Texas claims that it was injured because its former employees misbehaved during the course of their employment. The company has not reimbursed South Texas for this loss. The following motions are pending in this cause: (1) Defendant's motion for partial summary judg-

ment and motion to dismiss, (2) Defendant's motion for leave to amend, and (3) Defendant's motion to compel production of certain portions of federal examiners reports, filed August 24, 1984.

The company first asserts that South Texas cannot proceed under the Deceptive Trade Practices-Consumer Protection Act, Tex. Bus. & Com. Code Ann. § 17.41 et. seq. (Vernon Supp. 1984) (D.T.P.A.), because South Texas did not give the company written notice at least thirty (30) days before filing this lawsuit. Id., § 17.50A. This admitted failure to give notice, however, does not require dismissal or judgment for Defendant. When "defect in the notice . . . [is] . . . brought to the attention of the trial court before trial[,] . . . the trial court should . . . abate the proceeding for thirty (30) days." Hollingsworth Roofing Co. v. Morrison, 668 S.W.2d 872, 875 (Tex. Civ. App.—Ft. Worth 1984, no writ). The Court would therefore be inclined to abate this action for thirty (30) days to allow the proper notice to be given. A serious question exists, however, as to the validity of a claim directly under the DTPA.

In the first place, it seems from South Texas' responsive brief that it intends to proceed instead under § 16 of article 21.21 of the Insurance Code. Section 16 provides a cause of action to remedy unlawful deceptive trade practices defined in § 4 of the Insurance Code, or in § 17.46 of the DTPA, or in rules and regulations adopted by the State Board of Insurance. Although a plaintiff may not claim a breach of warranty or unconscionability under § 16, Mobile County Mut. Ins. Co. v. Jewell, 555 S.W.2d 903, 911 (Tex. Civ.-El Paso 1977); writ ref'd n.r.e., per curiam, 566 S.W.2d 295 (Tex. 1978), it is not true—as contended by the company—that there is no private cause of action under § 16. See, Bragg, Maxwell, & Longley, TEXAS CONSUMER LITIGATION (2d Ed. 1983) § 7.03 (Consumer Litigation). Indeed the Texas Supreme

Court per curiam opinion refusing application for writ of error in Hi-Line Electric Company v. Travelers Insurance Cos., 587 S.W.2d 488 (Tex. Civ. App.-Dallas, 1979) writ ref. n.r.e., per curiam, 593 S.W.2d 953 (1980) was apparently written specifically to reject the lower court's holding that suit under article 21.21 of the Insurance Code must be based on the Deceptive Trade Practices Act.

The more difficult issue is which of the so-called "three prongs" described in § 16 apply to this case. The first prong refers to those practices defined in § 17.46 of the DTPA, and only those acts enumerated in § 17.46(b) may be considered. Mobile County Ins. Co. v. Jewell, supra. South Texas nowhere alleges in its Second Amended Original Complaint nor intimates in its brief which of the twenty-three specified acts applies to this case. The Court finds none to be applicable, including those specifically discussed by Judge Higginbotham in Jay Freeman Co. v. Glens Falls Ins. Co., 486 F.Supp. 140 (N.D. Tex. 1980). Likewise, under the second prong, nothing in § 4 of article 21.21 seems to apply to these facts. In its brief, South Texas relies primarily on the third prong, namely a practice condemned by "rules or regulations lawfully adopted" by the State Board. Specifically, South Texas invokes Regulation No. 18663, dated December 3, 1971.

Admittedly that Regulation, particularly sections 4 and 5 thereof, contains some rather sweeping definitions of unfair trade practices and misrepresentations. See, Consumer Litigation at § 7.04. Nevertheless, despite the Regulation, subsequent Texas cases have consistently held that denial of liability by an insurance company after the loss has occurred is not actionable under either the DTPA or article 21.21 of the Insurance Code. American Ins. Cos. v. Reed, 626 S.W.2d 898, 905 (Tex. Civ. App.—Eastland, 1981, no writ); General Acc. Fire & Life Assur. Corp., Ltd. v. Legate, 578 S.W.2d 505, 507 (Tex. Civ.

App.—Texarkana, 1979, writ ref'd n.r.e.); Lone Star Life Ins. Co. v. Griffin, 574 S.W.2d 576, 580 (Tex. Civ. App.—Beaumont, 1978, writ ref'd n.r.e.). South Texas attempts to distinguish these cases by defining its complaint to be not of a mere denial of coverage but rather of alleged misrepresentations pertaining to such things as when the Company would complete its post-loss investigation and make a decision on the claim. The Court finds this to be a distinction without a difference, particularly in view of the rationale of the above cited cases, namely that a post-loss denial of benefits does not terminate the Company's obligations or extinguish the insured's rights. Also there is no allegation that South Texas did anything in reliance on the alleged misrepresentations or was injured by them in any way other than the injury that would always occur when an insured is not promptly paid its demand. See, *Royal Globe Ins. Co. v. Bar Consultants, Inc.*, 577 S.W.2d 688, 694 (Tex. 1979). It is therefore ORDERED that South Texas' claim under the DTPA and § 16 of article 21.21 of the Insurance Code be DISMISSED.

The Defendant Insurance company also seeks summary judgment on the grounds that South Texas did not comply with the policy provision requiring it to furnish a sworn written proof of loss within 100 days "after discovery of loss". The policy defines discovery as occurring "when the insured becomes aware of facts which would cause a reasonable person to assume that a loss covered by the bond has been or will be incurred, even though the exact amount of details of loss may not then be known." South Texas does not challenge the applicability of these policy provisions. Instead, the main thrust of its response is the invocation of the provisions of article 5546, V.A.T.S., providing that whenever an insurance contract requires notice as a condition precedent to the right to sue, it shall be presumed that such notice has been given unless

lack of notice is specially pleaded under oath. This suit is in federal court, however, and the Federal Rules of Civil Procedure contain a provision clearly applicable. Rule 9(c) provides merely that the denial of the performance of a condition precedent "shall be made specifically and with particularity." The Defendant has done this in its original answer and in all subsequent amendments.

This issue is controlled by Rosales v. Honda Motor Co., Ltd., 726 F.2d 259 (5th Cir. 1984). There the Court explained that when a federal rule is clearly applicable, the analysis in Hanna v. Plumer, 380 U.S. 460 (1965), applies. Under that test, this Court concludes that Rule 9(c) does not abridge, enlarge or modify any substantive right and is within the scope of the Rules Enabling Act and a constitutional grant of power. Thus the Court concludes that Rule 9(c), Fed. R. Civ. P., controls over Article 5546 V.A.T.S. In any event, the Defendant has tendered an amended answer which would also comply with the state rule and the Court will GRANT leave to file that amendment.

The issue then becomes whether, under the policy in question, timely filing of a proof of loss is a condition precedent to recovery. South Texas relies on Aetna Life Ins. Co. v. Tipps, 98 S.W.2d 375 (Tex. Civ. App.-El Paso 1976, no writ) for the proposition that an untimely filing does not prevent recovery in the absence of a specific policy provision declaring a forfeiture. On the other hand, more recent authorities—including a decision by the Texas Supreme Court—appear to unequivocally hold that where an insurance contract requires proof of loss, a claimant's timely compliance with that requirement is a condition precedent to recovery. United States Fidelity and Guaranty Co. v. Bimco Iron & Metal Corp., 464 S.W.2d 353 (Tex. 1971); General American Life Ins. Co. v. Rodriquez, 641 S.W.2d 264, 269 (Tex. Civ. App.-Houston [14th Dist.] 1982, no writ). Unfortunately, neither of

those decisions contains the wording of the proof of loss provision actually being considered. In Anchor Casualty Company v. Bowers, 385 S.W.2d 568 (Tex. Civ. App.-Houston 1964), rev'd on other grounds, 393 S.W.2d 168 (Tex. 1965) (approves proof of loss analysis), the court held that "where an insurance policy makes the furnishing of a proof of loss a condition precedent to the enforcement of the policy," failure to comply bars recovery. Id. at 569. Again, however, the decision fails to describe the policy provision in that case, thus shedding little light on the question of what language is necessary to "make" the timely filing of a proof of loss a condition precedent to recovery. That question is not easily answered, as evident from the many conflicting statements and citations contained in COUCH ON INSURANCE 2d (Rev. ed.), § 49.

One Texas decision which does contain the pertinent policy language is Federal Surety Co. v. Smith, 41 S.W.2d 210 (Tex. Comm'n App. 1931, holding approved). The policy there required, inter alia, that proof of loss must be filed within ninety days after the date of the loss and that no action "shall be brought to recover on this policy prior to the expiration of forty days after proof of loss has been filed in accordance with the requirements of this policy." Id. at 212. The court concluded that this was a valid condition precedent with which the insured must comply in order to recover. The instant policy, in Section 5 of its general conditions and limitations, contains similar language. It provides that the insured shall furnish a sworn proof of loss within six months after discovery of the loss and that legal proceedings for the recovery of any loss shall not be brought prior to the expiration of sixty days after the filing of the proof of loss. Based on Federal Surety Co. v. Smith, supra, and other cases cited above, the Court would be inclined to hold that this language made the timely filing of a proof of loss a binding condition precedent to recovery. It appears, however, that

this language in Section 5 may have been superseded. The Defendant urges, and South Texas does not challenge, that a separate rider governs this point. That rider purports to be controlling despite anything to the contrary in the attached bond. The rider provides that proof of loss shall be made within 100 days after discovery of loss and that legal proceedings for recovery of the loss shall not be brought after the expiration of 28 months "after the cause of action shall have accrued." The provision that legal proceedings shall not be brought prior to sixty days after the filing of the proof of loss is eliminated, and the rider appears to sever the previous interrelationship between the requirement for filing a proof of loss and the actual filing of suit.

This rider causes the Court to raise the question of whether the proof of loss requirement in the rider is indeed a condition precedent to recovery. The Court invites further briefing on this point, not only as to any legal authorities, but also the circumstances surrounding the insertion of the rider into the policy and why it removes the provision that suit may not be filed until a specified period after the filing of the proof of loss.

This issue is potentially quite significant because South Texas, in its reply brief, apparently concedes that its proof of loss was not filed until June 24, 1982. Defendant company insists that this date is more than 100 days after South Texas became aware of facts which would cause a reasonable person to assume that an insured loss had occurred. Although the Court is not prepared to so rule as a matter of law at this time, this argument is not without some force. The Court particularly refers to the evidence that on February 23, 1982, the directors of South Texas authorized the bank's attorney "to calculate the loss resulting from the Lerma indebtedness and to submit a claim to the company for the full amount of the claim." It is difficult to imagine how South Texas could not have

discovered the Lerma loss when its directors officially voted to file a claim for that precise loss. On the other hand, the fact that the directors had knowledge of some irregularities and violations would not itself trigger the obligation to notify the company because of the rule that notice is not required until the bank has knowledge of "some specific fraudulent or dishonest act." Federal Deposit Insurance Corp. v. Lott, 460 F.2d 82, 87 (5th Cir. 1972). It is undisputed that South Texas had knowledge of at least two specific dishonest acts by Bristow no later than early February 1982 (see Exhibits Z1-3, Deposition of Fernando F. Zuniga). but it is not clear that these acts pertained to Francisco Lerma or whether they are the subject of the instant claim. The only specific act of misconduct that the Court can glean from the Second Amended Original Complaint is that Bristow was being given money, gold and automobile in return for making bad loans. Douglas G. McDonald has furnished an affidavit stating that the bank did not learn of these facts until April 2, 1982. If that be true, and if those are the only specific acts of misconduct known to the bank, the proof of loss may well be timely. The ultimate question would not be when the bank reasonably discovered a loss, but when it reasonably discovered a loss covered by the policy.

SUMMARY

The claim by South Texas for treble damages under the DTPA and under the Insurance Code is DISMISSED. Defendant's motion for leave to file its third amended answer is GRANTED. After reflecting on this memorandum, Defendant shall determine whether it still wishes to pursue the contention that the proof of loss was not timely filed. If so, Defendant shall file no later than February 1, 1985 a supplemental brief addressing the

questions of whether or not the proof-of-loss provision in this particular policy is a binding condition precedent and when South Texas acquired knowledge of some specific fraudulent or dishonest act related to the Lerma transactions. South Texas may reply on or before twenty five (25) days thereafter. The Court shall defer resolution of the dispute over discovering the Federal Examiner's reports until the foregoing issues are resolved.

APPENDIX C

COURT OF APPEALS
FIRST SUPREME JUDICIAL DISTRICT

NO. 01-85-0159-CV

GLEN ARNOLD, Appellant

v.

NATIONAL COUNTY MUTUAL FIRE INSURANCE COMPANY, Appellee

OPINION

On Appeal from the 151st District Court of Harris County, Texas Trial Court Cause No. 78-52226

The plaintiff, Glen Arnold, appeals from a take-nothing summary judgment, entered in favor of the defendant, National County Mutual Fire Insurance Company. We affirm.

In June 1974, Arnold was severely injured when the motorcycle he was driving was struck by a car driven by an uninsured motorist. Arnold was insured by National County Mutual under a policy that included "uninsured motorist" protection with a limit of $10,000. Arnold made timely demand for payment of the $10,000 limit, and an independent insurance adjusting firm employed by National County Mutual recommended, within six months following the date of the accident, that National County Mutual pay the entire policy limit to Arnold. But National County Mutual refused to pay, and Arnold filed suit against the uninsured motorist and National County Mutual. In December 1977, Arnold obtained a judgment against the uninsured motorist and National County Mutual in the amount of $17,974.75. National County Mutual then paid Arnold the $10,000 policy limit of his uninsured motorist coverage. Arnold filed this suit on December 27, 1978, alleging National County Mutual's

bad faith in handling his claim. On November 26, 1984, the trial court granted National County Mutual's motion for summary judgment.

In its motion for summary judgment, National County Mutual alleged four principal grounds of defense. It asserted: (1) that because it was a county mutual insurance company, it was not subject to the provisions of the Texas Insurance Code, specifically, article 21.21 (Vernon 1981), or the Deceptive Trade Practices-Consumer Protection Act, Tex. Bus. & Com. Code Ann. secs. 17.41-17.63 (Vernon Supp. 1985), under which Arnold sued (2) that Arnold did not have a private right of action under the Unfair Claim Settlement Practices Act, Tex. Ins. Code Ann. art. 21.21-2 (Vernon 1981); (3) that under Texas law, there was no implied covenant of good faith and fair dealing in its insurance contract with Arnold, and therefore, regardless of motive, the company's handling of Arnold's claim created no cause of action for bad faith; and finally, (4) that Arnold's causes of action, if any, were barred by the applicable statutes of limitations, Tex. Rev. Civ. Stat. Ann. arts. 5526, 5527 (Vernon 1958). The trial court's judgment does not state the particular grounds upon which the judgment was entered. We must therefore examine the judgment in light of the grounds of defense set forth in the motion for summary judgment or raised in the appellant's response thereto.

We conclude that Arnold's suit is barred by limitations, as asserted under the fourth ground of defense in the motion for summary judgment, and so we need not consider the other issues.

Both in his pleadings and in his brief on appeal, Arnold contends that National County Mutual wrongfully refused to pay his claim within six months from the date of the accident on June 1, 1974. Assuming that National County Mutual's refusal to pay Arnold's uninsured moto-

rist claim gave him a cause of action, Arnold's rights were invaded at the time his claim was rejected.

This is not a "Stowers" case, as the appellant contends, where the statute of limitations begins to run when a judgment in favor of a third party is entered against the plaintiff in excess of his policy limits. *See Linkenhoger v. American Fidelity & Casualty Co.,* 260 S.W.2d 884, 887 (Tex. 1953); *see also G. A. Stowers Furniture Co. v. American Indemnity Co.,* 15 S.W.2d 544 (Tex. Comm'n App. 1929, opinion adopted). In a "Stowers" situation, the liability of the plaintiff's insurer arises because of its previous negligent rejection of the third party's settlement offer, which was within the insured plaintiff's policy limits. There, the plaintiff's damages cannot be determined until the judgment in excess of his policy limit is entered against him.

In the case at bar, the appellant's entire cause of action is based on the contention that National County Mutual wrongfully refused to pay his own claim at a certain time, i. e., within six months after the accident. A cause of action accrues, and limitations begin to run, when facts exist that authorize the person asserting a claim to seek relief in a court of competent jurisdiction, *Linkenhoger,* 260 S.W.2d at 886, and not, as the appellant contends, when a court finally determines that those facts do indeed entitle the plaintiff to relief.

Arnold did not file this suit until December 27, 1978, more than four years after the appellee's allegedly wrongful refusal to pay his claim, and therefore, his asserted causes of action, both in tort and arising from his insurance contract, are barred by limitations. Arts. 5526, 5527.

The judgment of the trial court is affirmed.

/s/ FRANK G. EVANS

FRANK G. EVANS
Chief Justice

Associate Justices Bass and Cohen also sitting.
No publication.

Judgment rendered and opinion delivered August 22, 1985.

True copy attest;

KATHRYN COX

Kathryn Cox
Clerk of the Court

Supreme Court, U.S.
FILED
NOV 17 1986
JOSEPH F. SPANIOL, JR.
CLERK

NO. 86-583

IN THE

Supreme Court of the United States

OCTOBER TERM, 1986

JIM AUSTIN AND AULEMIC, INC.,
Petitioners,

v.

LEXINGTON INSURANCE COMPANY,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

REPLY MEMORANDUM

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REPLY MEMORANDUM

In the Petition for a Writ of Certiorari, we showed that by reaching out to decide a question of Texas state law pending before that state's highest court, the United States Court of Appeals for the Fifth Circuit violated fundamental principles of federalism. Respondent's Brief in Opposition demonstrates the validity of this point and the necessity that the petition be granted.

Respondent's brief is devoted almost entirely to an exposition of the conflicting decisions rendered by the intermediate appellate courts of the state of Texas and of the federal district courts in Texas interpreting the provisions of the Texas Insurance Code relied upon by Petitioners in seeking damages for Respondent's unfair claims handling practices. Although Respondent attempts to harmonize some of the conflicting decisions and distinguish those which reject his theories, he admits that "the rationale of each case and the precise holdings vary."[1] What Respondent fails to tell this Honorable Court, however, is that the Texas Supreme Court has granted writs of error in several cases[2] in order to resolve the conflicting opinions of the lower courts throughout

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1. Respondent's Brief in Opposition at page 4.

2. The Texas Supreme Court has granted writs of error to review the following decisions:

Chitsey v. National Lloyds Insurance Company, 698 S.W.2d 766 (Tex. App.—Austin 1985, writ of error granted), 29 Tex. Sup. Ct. J. 390 (May 28, 1986), a case cited by Respondent, Lexington and the court of appeals for the proposition that Texas law does not provide a private cause of action for treble damages under Art. 21.21 for unfair claims settlement practices.

Arnold v. National County Mutual Fire Insurance Co., (Tex. App. —Houston [1st Dist.] August 22, 1985, writ granted), 29 Tex. Sup. Ct. J. 78 (Nov. 27, 1985), a case where Plaintiff was denied a private cause of action for unfair claims settlement practices under Art. 21.21.

Aetna Casualty and Surety v. Marshall, 699 S.W.2d 896 (Tex. App.—Houston [1st Dist.] 1985, writ granted), 29 Tex. Sup. Ct. J. 532 (July 16, 1986), a case where Plaintiff was awarded treble damages against his workers' compensation insurance carrier for unfair claims settlement practices under Art. 21.21.

Writ of error appeals are pending before the Texas Supreme Court in the following case:

Texas Farm Bureau Mutual Insurance Co. v. Vail, 659 S.W.2d 692 (Tex. App.—Dallas 1985, writ requested), a case where Plaintiff was denied treble damages under Art. 21.21 for unfair claims settlement practices.

this entire field of insurance law. Particularly important is the fact that a key case relied on by the Fifth Circuit, *Chitsey v. National Lloyds Insurance Company,*[3] was briefed and orally argued to the Texas Supreme Court *prior* to the decision of the Fifth Circuit below.

For the Fifth Circuit to render a decision on a matter of Texas law which the Texas Supreme Court has agreed to hear as a part of its consideration of several important points of Texas law is not only disrespectful of the function of the role of that state's highest court in developing Texas law,[4] but may also prove to be an embarrassment to the federal judiciary if the ruling of the court of appeals turns out to be incorrect. *See Railroad Commission of Texas v. Pullman Co.,* 312 U.S. 496, 500 (1941). The fact that the Texas Supreme Court has granted writs of error in several of these cases in this area in order to resolve the conflicting opinions in an entire field of insurance law, including the precise question at issue in this case, should control the disposition of this appeal.

Instead of divining state law questions which are pending before the state's highest court, the court of appeals should have stayed its action pending the decision of the state supreme court, or more appropriately, certified the question of state law to the state supreme court to decide in conjunction with its consideration of the entire field of law. To make an advance guess as to the

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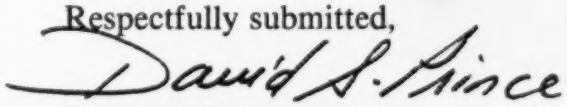
3. 698 S.W.2d 766 (Tex. App.—Austin, writ of error granted), 29 Tex. Sup. Ct. J. 390 (May 28, 1986).

4. "National Government will fare best if the States and their institutions are left free to perform their separate functions in their separate ways." *Younger v. Harris,* 401 U.S. 37, 44 (1971).

result, or worse—to ignore all of the decisions of the state's highest court as the court of appeals did in this case—is an unconstitutional and unnecessary interference by the federal court with the development of state law and with the interpretation of the statutes of the Texas legislature. Furthermore, the Fifth Circuit's decision on a question of state law which is pending before the Texas Supreme Court is prejudicial to the litigants by giving them "a ticket for one ride only." Brown, Certification—Federalism in Action, 7 CUMBERLAND L. REV. 455, 456 (1977).

For the reasons stated herein and in the Petition for a Writ of Certiorari, Petitioner respectfully submits that the Petition should be granted.

Respectfully submitted,



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